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BEFORE THE ARIZONA CORPORATION COMMISSION

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IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY,  
AN ARIZONA CORPORATION, FOR A  
DETERMINATION OF THE CURRENT FAIR  
VALUE OF ITS UTILITY PLANT AND  
PROPERTY AND FOR INCREASES IN ITS  
RATES AND CHARGES BASED THEREON  
FOR UTILITY SERVICE BY ITS ANTHEM  
WATER DISTRICT AND ITS SUN CITY  
WATER DISTRICT.

Docket No. W-01303A-09-0343

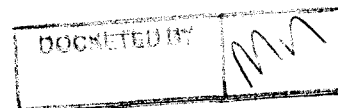
IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY,  
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FOR UTILITY SERVICE BY ITS  
ANTHEM/AGUA FRIA WASTEWATER  
DISTRICT, ITS SUN CITY WASTEWATER  
DISTRICT AND ITS SUN CITY WEST  
WASTEWATER DISTRICT.

Docket No. SW-01303A-09-0343

Arizona Corporation Commission

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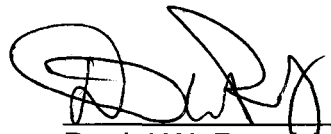
APR 15 2010



RUCO'S NOTICE OF FILING  
SURREBUTTAL TESTIMONY

1 The Residential Utility Consumer Office ("RUCO") hereby provides notice of filing  
2 the Surrebuttal Testimony of William A. Rigsby, CRRRA, and Ralph C. Smith in the above-  
3 referenced matter.

4 RESPECTFULLY SUBMITTED this 15th day of April, 2010.

5  
6  
7 

8 Daniel W. Pozersky  
9 Chief Counsel

10  
11 AN ORIGINAL AND THIRTEEN COPIES  
12 of the foregoing filed this 15th day  
13 of April, 2010 with:

14 Docket Control  
15 Arizona Corporation Commission  
1200 West Washington  
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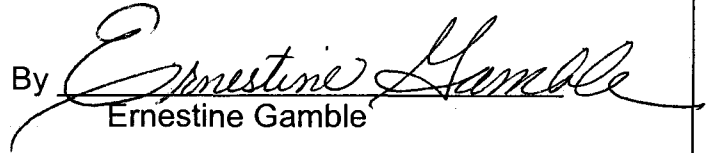
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17 mailed this 15th day April, 2010 to:

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**ARIZONA-AMERICAN WATER COMPANY**

**DOCKET NO. W-01303A-09-0343  
AND DOCKET NO. SW-01303A-09-0343**

**SURREBUTTAL TESTIMONY**

**OF**

**WILLIAM A. RIGSBY**

**ON BEHALF OF**

**THE**

**RESIDENTIAL UTILITY CONSUMER OFFICE**

**APRIL 15, 2010**



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5  
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**TABLE OF CONTENTS**

INTRODUCTION..... 1

SUMMARY OF AAWC'S REBUTTAL TESTIMONY..... 3

INFRASTRUCTURE SYSTEM REPLACEMENT SURCHARGE ..... 4

REBUTTAL TO ANTHEM COMMUNITY COUNCIL ..... 6

**INTRODUCTION**

Q. Please state your name, occupation, and business address.

A. My Name is William A. Rigsby. I am a Public Utilities Analyst V employed by the Residential Utility Consumer Office ("RUCO") located at 1110 W. Washington, Suite 220, Phoenix, Arizona 85007.

Q. Please state the purpose of your surrebuttal testimony.

A. The purpose of my surrebuttal testimony is to respond to Arizona-American Water Company, Inc.'s ("AAWC" or "Company") witness Paul G. Townsley's rebuttal testimony filed on March 22, 2010. My surrebuttal testimony will address the Company-proposed infrastructure improvement surcharge for the AAWC's Sun City Water District. Furthermore, the Company has stated that if rate consolidation is adopted by the ACC in this proceeding it proposes to expand the infrastructure improvement surcharge for all of its districts in Arizona.

Q. Have you filed any prior testimony in this case on behalf of RUCO?

A. Yes, on March 8, 2010, I filed direct testimony with the Commission on this specific issue. I also filed, under separate cover, direct testimony on the cost of capital issues in this case.

...

1 Q. Are you also filing surrebuttal testimony on the cost of capital issues in this  
2 case?

3 A. Yes. I have also filed a separate piece of surrebuttal testimony on the  
4 cost of capital issues in this case.

5  
6 Q. Will RUCO be filing surrebuttal testimony on the rate base and operating  
7 income issues in this case?

8 A. Yes. RUCO's outside consultant Mr. Ralph Smith, will file surrebuttal  
9 testimony on the rate base and operating income issues in this case.

10  
11 Q. Is RUCO filing rate design testimony in this proceeding?

12 A. Yes. In accordance with the Administrative Law Judge's Procedural  
13 Order dated March 18, 2010, both RUCO Director Jodi Jerich, Esq. and  
14 RUCO analyst Rodney L. Moore will provide direct testimony on RUCO's  
15 rate consolidation policy and RUCO's recommended rate design  
16 respectively on May 3, 2010. Ms. Jerich and Mr. Moore will offer their  
17 surrebuttal testimony, on rate consolidation policy and rate design, orally  
18 at the evidentiary hearing scheduled for May 18, 2010.

19  
20 Q. How is your surrebuttal testimony organized?

21 A. My surrebuttal testimony contains four parts: the introduction that I have  
22 just presented; a summary of Mr. Townsley's rebuttal testimony; a section  
23 that discusses RUCO's surrebuttal position on the Company-proposed

1           infrastructure improvement surcharge; and a response to the testimony of  
2           Anthem Community Council's witness, Dan Neidlinger.

3  
4   **SUMMARY OF AAWC'S REBUTTAL TESTIMONY**

5   Q.    Have you reviewed the rebuttal testimony of Mr. Paul G. Townsley that  
6           addresses the Company-proposed infrastructure improvement surcharge  
7           for the AAWC's Sun City Water District?

8   A.    Yes. I have reviewed Mr. Townsley's rebuttal testimony that addresses  
9           the Company-proposed infrastructure improvement surcharge for AAWC's  
10          Sun City Water District.

11  
12   Q.    Please summarize the Company's rebuttal testimony.

13   A.    In his rebuttal testimony, Mr. Townsley adopts the direct testimony of  
14          Company witness Christopher C. Buls who originally addressed the  
15          infrastructure improvement surcharge for the Sun City Water District. Mr.  
16          Townsley refers to the Company-proposed surcharge as an Infrastructure  
17          System Replacement Surcharge ("ISRS") and states that I was the only  
18          witness that responded to the Company's request and the only witness  
19          that recommended that the Company-proposed ISRS be rejected by the  
20          Commission. Mr. Townsley disagrees with RUCO's recommendation to  
21          reject the ISRS and also disagrees with my statements that the plant  
22          additions would be financed by non-investor supplied funds. Mr. Townsley

continues to advocate that the ISRS be expanded to all of the Company's Districts if the Commission orders full rate consolidation.

**INFRASTRUCTURE SYSTEM REPLACEMENT SURCHARGE**

Q. Do you agree with Mr. Townsley's position that the costs for plant additions, which AAWC would be recovering through the Company-proposed ISRS, would be funded by investor supplied capital?

A. Technically, yes. I have reconsidered my position on this point and I agree with Mr. Townsley that the costs for plant additions would initially be funded up front by investor supplied capital. However, funds collected through the ISRS would repay the Company for its up-front investment for routine plant additions.

Q. Does RUCO still recommend that the Commission reject the Company-proposed ISRS?

A. Yes. With the exception of those portions of my direct testimony regarding non-investor supplied capital addressed above, RUCO believes that all of the reasons RUCO provided for rejecting the Company-proposed ISRS are valid and continues to advocate that the Commission should reject the ISRS. Nothing in Mr. Townsley's rebuttal testimony changes RUCO's position.

1 Q. Do you agree with Mr. Townsley's statement that you were the only  
2 witness that responded to the Company's request, and the only witness  
3 that recommended that the Company-proposed ISRS be rejected by the  
4 Commission?

5 A. Yes and No. When Mr. Townsley filed his rebuttal testimony, I was the  
6 only witness in this proceeding to address the ISRS and to recommend  
7 that it be rejected by the Commission. However, since that time ACC Staff  
8 witness Mr. Jeffery Michlik has filed direct testimony on rate design which  
9 addresses the ISRS issue and also recommends that the Company-  
10 proposed ISRS be rejected by the Commission. Mr. Michlik states that  
11 "The Company has offered no explanation why these ordinary  
12 infrastructure improvements or replacements should be handled in this  
13 extraordinary fashion." Mr. Michlik goes on to say that ACC Staff  
14 "believes that such ordinary infrastructure improvements should be  
15 handled in the normal fashion through inclusion in rate base in future rate  
16 filings as appropriate." Mr. Michlek further states that "The Commission  
17 has rejected such requests for extraordinary treatment in the past." In  
18 short Mr. Michlek's testimony echoes the reasons that I presented in my  
19 direct testimony for rejection of the Company-proposed ISRS.

20  
21  
22 ...  
23

1 Q. So RUCO still recommends that the Commission reject the Company-  
2 proposed ISRS?

3 A. Yes. RUCO's position has not changed. As I stated in my direct  
4 testimony, there is no federal, or for that matter any other, mandates  
5 requiring that AAWC be required to construct the types infrastructure  
6 improvements that would be covered under the ISRS. Nor are there any  
7 other extraordinary circumstances that would warrant the approval of an  
8 ACRM-like mechanism that would allow the Company to recover costs  
9 associated with routine plant additions that would normally be subject to  
10 much closer scrutiny during a general rate case proceeding.  
11

12 **REBUTTAL TO ANTHEM COMMUNITY COUNCIL**

13 Q. What is your response to Anthem Community Council's witness Daniel  
14 Neidlinger's testimony that the Council intends to challenge the legal basis  
15 for AAWC's proposed inclusion of the March 2008 \$20.2 million AIAC  
16 payment to Pulte Homes in rate base for ratemaking purposes in this  
17 proceeding?

18 A. Like Mr. Neidlinger, I am not an attorney and able to give a legal opinion.  
19 RUCO has not challenged the recovery of the refunds or the rate base  
20 treatment of the assets in its direct case. However, RUCO has instructed  
21 me that RUCO reserves the right to modify its position on this issue should  
22 the legal argument prove valid. RUCO is in the process of doing its own  
23 investigation into the facts and circumstances of that argument and may or

1           may not supplement its testimony depending on the results of its  
2           investigation.

3  
4   Q.    Does your silence on any of the issues, matters or findings addressed in  
5           the rebuttal testimony of any of the witnesses for AAWC constitute your  
6           acceptance of their positions on such issues, matters or findings?

7   A.    No, it does not.

8  
9   Q.    Does this conclude your surrebuttal testimony on the Company-proposed  
10          ISRS?

11   A.    Yes, it does.



**ARIZONA-AMERICAN WATER COMPANY**

**DOCKET NO. W-01303A-09-0343  
AND DOCKET NO. SW-01303A-09-0343**

**SURREBUTTAL TESTIMONY  
ON COST OF CAPITAL**

**OF**

**WILLIAM A. RIGSBY**

**ON BEHALF OF**

**THE**

**RESIDENTIAL UTILITY CONSUMER OFFICE**

**APRIL 15, 2010**

1

## TABLE OF CONTENTS

2

INTRODUCTION..... 1

3

SUMMARY OF AAWC's REBUTTAL TESTIMONY ..... 2

4

CAPITAL STRUCTURE ..... 3

5

COST OF DEBT..... 4

6

COST OF EQUITY CAPITAL ..... 5

7

ATTACHMENT A

8

ATTACHMENT B

1 **INTRODUCTION**

2 Q. Please state your name, occupation, and business address.

3 A. My name is William A. Rigsby. I am a Public Utilities Analyst V employed  
4 by the Residential Utility Consumer Office ("RUCO") located at 1110 W.  
5 Washington, Suite 220, Phoenix, Arizona 85007.

6  
7 Q. Please state the purpose of your surrebuttal testimony.

8 A. The purpose of my testimony is to comment on the proposed agreement  
9 between Arizona-American Water Company, Inc.'s ("AAWC" or  
10 "Company") rebuttal testimony on RUCO's recommended rate of return on  
11 invested capital (which includes RUCO's recommended capital structure,  
12 cost of long-term debt and cost of common equity) for the two water  
13 districts and three wastewater districts that AAWC is seeking rate  
14 increases for in this proceeding.

15

16 Q. Have you filed any prior testimony in this case on behalf of RUCO?

17 A. Yes, on March 8, 2010, I filed direct testimony with the Commission on the  
18 cost of capital issues in this case. I also filed, under separate cover, direct  
19 testimony on AAWC's request for an infrastructure improvement  
20 surcharge.

21

22

23

1 Q. Are you also filing surrebuttal testimony on the infrastructure improvement  
2 surcharge that the Company is requesting in this case?

3 A. Yes. I have also filed a separate piece of surrebuttal testimony on the  
4 infrastructure improvement surcharge issue.

5  
6 Q. How is your surrebuttal testimony on cost of capital organized?

7 A. My surrebuttal testimony contains five parts: the introduction that I have  
8 just presented; a summary of AAWC's rebuttal testimony; a section on  
9 capital structure; a section on the cost of debt; and, a section on the cost  
10 of equity capital.

11  
12 **SUMMARY OF AAWC's REBUTTAL TESTIMONY**

13 Q. Have you reviewed AAWC's rebuttal testimony?

14 A. Yes. I have reviewed the rebuttal testimony of Company witnesses,  
15 Thomas M. Broderick and Dr. Bente Villadsen, filed on March 22, 2009,  
16 which address the cost of capital issues in this case.

17  
18 Q. Please summarize the Company's rebuttal testimony.

19 A. Mr. Broderick's rebuttal testimony states that AAWC has accepted ACC  
20 Staff's recommended 7.2 percent weighted average cost of capital  
21 including ACC Staff's recommended capital structure, cost of short-term  
22 and long-term debt, and cost of common equity. In light of the fact that  
23 AAWC has abandoned her cost of capital recommendations, Dr. Villadsen

devotes her entire rebuttal testimony to my recommended cost of common equity. She states why she believes my recommended 9.50 percent cost of common equity is not reasonable and makes adjustments to the models that I have used in my cost of equity analysis.

## CAPITAL STRUCTURE

Q. Please compare the capital structure recommendations of ACC Staff and RUCO.

A. A comparison of ACC Staff and RUCO's capital structures are as follows:

### ACC Staff

Short & Long-Term Debt	61.14%
Common Equity	38.86%

### RUCO

Short-Term Debt	13.29%
Long-Term Debt	47.56%
Common Equity	39.15%

As can be seen above there is very little difference between the capital structures being recommended by ACC Staff witness Juan C. Manrique and myself. Mr. Manrique's capital structure contains slightly less debt than the capital structure that I am recommending.

**COST OF DEBT**

Q. Have you made any changes to your recommended costs of short-term and long-term debt?

A. No, I have not.

Q. Please compare the costs of long-term debt being recommended by ACC Staff and RUCO for AAWC.

A. ACC Staff and RUCO are recommending the following:

ACC Staff

Short & Long-Term Debt	4.91%
------------------------	-------

RUCO

Short-Term Debt	3.91%
-----------------	-------

Long-Term Debt	5.47%
----------------	-------

Q. What is the difference between ACC Staff's recommended cost of debt and RUCO's recommended cost of debt?

A. As can be seen above ACC Staff's Mr. Manrique has elected to combine his recommended costs of short-term and long-term debt into a single weighted cost of debt of 4.91 percent.

1 Q. What would the weighted cost of RUCO's recommended costs of short-  
2 term and long-term be if you took the same approach as Mr. Manrique  
3 has?

4 A. RUCO's weighted cost of debt would be 5.02 percent, or eleven basis  
5 points higher than ACC Staff's weighted cost of debt, and would produce  
6 the same weighted average cost of capital that I am recommending in this  
7 case.

8  
9 **COST OF EQUITY CAPITAL**

10 Q. Have you made any changes to the 9.50 percent cost of common equity  
11 that you recommended in your direct testimony?

12 A. No.

13  
14 Q. What costs of equity capital are ACC Staff and RUCO recommending?

15 A. The costs of common equity presently being recommended by ACC Staff  
16 and RUCO are as follows:

17		
18	ACC Staff	10.70%
19	RUCO	9.50%
20		

21 Presently there is a 120 basis point difference between our respective  
22 recommended costs of common equity.

1 Q. What are the weighted average costs of capital ("WACC") presently being  
2 recommended by ACC Staff and RUCO?

3 A. The WACC presently being recommended by ACC Staff and RUCO are  
4 as follows:

5		
6	ACC Staff	7.20%
7	RUCO	6.77%
8		

9 As can be seen above, there is a 43 basis point difference between Mr.  
10 Manrique's recommended WACC and my recommended WACC.

11  
12 Q. Has there been any recent activity in regard to interest rates?

13 A. Yes. On March 16, 2010, the Federal Reserve decided not to increase or  
14 decrease the federal funds rate and kept it between zero and 0.25  
15 percent. According to the minutes to the Federal Open Market  
16 Committee's meeting, the Fed affirmed its plan to keep interest rates  
17 "exceptionally low" for a long time as evidenced in this excerpt:

18 The Committee will maintain the target range for the federal  
19 funds rate at 0 to ¼ percent and continues to anticipate that  
20 economic conditions, including low rates of resource utilization,  
21 subdued inflation trends, and stable inflation expectations, are  
22 likely to warrant exceptionally low levels of the federal funds rate  
23 for an extended period. To provide support to mortgage lending  
24 and housing markets and to improve overall conditions in private  
25 credit markets, the Federal Reserve has been purchasing \$1.25  
26 trillion of agency mortgage backed securities and about \$175  
27 billion of agency debt; those purchases are nearing completion,  
28 and the remaining transactions will be executed by the end of  
29 this month. The Committee will continue to monitor the economic  
30 outlook and financial developments and will employ its policy  
31



1 tools as necessary to promote economic recovery and price  
2 stability.<sup>1</sup>  
3

4 The next FOMC meeting is scheduled for April 27, 2010.  
5

6 Q. Please address Dr. Villadsen's argument that your recommended 9.50  
7 percent cost of common equity is too low to attract investors during a  
8 period of turbulence in the financial markets.

9 A. I would say that my 9.50 percent return on common equity for AAWC  
10 looks very attractive to investors considering the fact that, as of January  
11 22, 2010, Value Line's analysts are projecting a long-term (i.e. the 2012-  
12 2014 time frame) 8.00 percent return on book common equity for the  
13 water utility industry as a whole. Value Line's long-term return on  
14 common equity for American Water Works, the parent company of AAWC,  
15 is 6.00 percent (Attachment E of my direct testimony). My recommended  
16 9.50 percent cost of common equity is 350 basis points higher than Value  
17 line's long-term projection for the Company's parent.  
18

19 Q. How do you respond to Dr. Villadsen's position that investors are more  
20 wary of water company stocks, which have been traditionally viewed as  
21 safe investments, during periods of financial uncertainty?

22 A. My response is that the investment community doesn't seem to view  
23 AAWC's parent in that light. As can be seen in Attachment A of my

---

<sup>1</sup> Minutes of the Federal Open Market Committee meeting held on March 16, 2010  
<http://www.federalreserve.gov/monetarypolicy/files/fomcminutes20100316.pdf>

1 testimony, American Water Work's stock price has experienced a definite  
2 upward trend over the past year. AAWC's parent company increased in  
3 value from \$17.33 per share on April 23, 2009, to 21.48 per share on April  
4 13, 2010 which is higher than Aqua America's price per share of \$17.97.  
5 If anything, there clearly appears to be a demand for American Water  
6 Works shares despite the recent economic climate.

7

8 Q. What is your opinion of Dr. Villadsen's argument that water utilities are  
9 riskier despite the fact that their betas are falling?

10 A. Dr. Villadsen has testified in prior cases that water utility stocks were  
11 riskier as evidenced by the fact that their betas, which measure a  
12 security's risk in relation to the market as a whole, were increasing. I fail  
13 to see how water utilities are riskier now, given the fact that their betas are  
14 falling, because lower betas indicate lower risk in relation to the market as  
15 a whole.

16

17 Q. Please address Dr. Villadsen's criticism that your DCF estimates of  
18 external growth are also biased downward.

19 A. Dr. Villadsen has taken issue with my calculation of "v" for the external  
20 growth rate estimate portion of the DCF's growth component. This  
21 calculation takes into consideration the fact that, while in theory a utility's  
22 stock price should move toward a market to book ratio of 1.0 if regulators  
23 authorize a rate of return that is equal to a utility's cost of capital, in reality

1 a utility will continue to issue shares of stock that are priced above book  
2 value.

3 As pointed out by Dr. Villadsen, I explained in my direct testimony that this  
4 same assumption was incorporated into the DCF analysis performed by  
5 Mr. Stephen Hill, ACC Staff's cost of cost of capital witness, in a prior  
6 Southwest Gas rate case proceeding.<sup>2</sup> Mr. Hill used the same methods  
7 that I have used in arriving at the inputs for his DCF model. His final  
8 recommendation for Southwest Gas Corporation, which was adopted by  
9 the Commission, was largely based on the results of his DCF analysis,  
10 which incorporated the same valid market-to-book ratio assumption that I  
11 have used consistently in cases before the Commission.

12  
13 Q. Please explain why a utility's stock will tend to move toward book value, or  
14 a market-to-book ratio of 1.0, if regulators allow a rate of return that is  
15 equal to the cost of capital of firms with similar risk.

16 A. As I stated in my direct testimony, the market value of a utility's stock will  
17 tend to move toward book value, or a market-to-book ratio of 1.0, if  
18 regulators allow a rate of return that is equal to the cost of capital of firms  
19 with similar risk. This premise is recognized among practitioners who  
20 have testified in cost of capital proceedings<sup>3</sup>.

---

<sup>2</sup> Docket No. G-01551A-04-0876

<sup>3</sup> Carleton, Willard T. and Morin, Roger A.

1 Despite Dr. Villadsen's criticism of my DCF methodology in her rebuttal  
2 testimony, I believe that a utility's market price should equal its book price  
3 over the long run if regulators allow a rate of return that is equal to the  
4 utility's cost of capital. That is assuming that the utility's rate of return  
5 ("ROR") is comparable to the rates of return of other firms in the same risk  
6 class. I believe that a better explanation of this concept is one that I have  
7 used in the past and assumes that if a hypothetical utility's book price is  
8 \$20.00 per share and regulators adopt a rate of return that is equal to the  
9 utility's cost of capital of 10.00 percent, the utility will earn \$2.00 per share  
10 ("EPS"). With earnings of \$2.00 per share, and a market required rate of  
11 return on equity of 10.00 percent, for firms in the utility's risk class, the  
12 market price of the utility's stock will set at \$20.00 per share ( $\$2.00 \text{ EPS} \div$   
13  $10.00\% \text{ ROR} = \$20.00 \text{ per share price}$ ). If the utility records earnings that  
14 are higher than the earnings of other firms with similar risk, the market  
15 value of the utility's shares will increase accordingly ( $\$2.50 \text{ EPS} \div 10.00\%$   
16  $\text{ROR} = \$25.00 \text{ per share}$ ). On the other hand, if the utility posts lower  
17 earnings, the stock's market price will fall below book value ( $\$1.50 \text{ EPS} \div$   
18  $10.00\% \text{ ROR} = \$15.00 \text{ per share}$ ).

19 Because of economic forces beyond the control of regulators, it is not  
20 reasonable to assume that the utility will have earnings that match those  
21 of firms of similar risk in every year of operation. In some years, earnings  
22 may drop causing the market-to-book ratio to fall below 1.0, while in other  
23 years the utility may have earnings that exceed those of other firms in its

1 risk classification. However, over the long run the utility's earnings should  
2 average out to the earnings that are expected based on its level of risk.  
3 These average earnings over time will result in a market-to-book ratio of  
4 1.0. A 1.0 ratio may never be achieved in practice and many investors  
5 may not even care what the market-to-book ratio is as long as they  
6 receive their required rate of return.

7

8 Q. Are there any other reasons why your market-to-book ratio calculation that  
9 is valid?

10 A. Yes. Each of the other utilities included in my sample, are engaged in  
11 unregulated activities to some degree. Because it is difficult to obtain a  
12 sample comprised only of "pure play" utilities, the calculation that I have  
13 employed in my DCF model helps to eliminate the impact that those  
14 unregulated operating segments would have on the market-to-book ratio  
15 of the utilities included in my sample.

16

17 Q. Please respond to Dr. Villadsen's argument that your overall CAPM  
18 results are below the current yields on Baa/BBB debt instruments.

19 A. I am not recommending that the Commission adopt my CAPM results. I  
20 am recommending a cost of common equity of 9.50 percent which is 315  
21 to 359 basis points over the most recent yields of 6.35 percent to 5.91  
22 percent for Baa/BBB-rated and A-rated utility bonds respectively  
23 (Attachment B).

1 Q. Is Dr. Villadsen correct in her assertion that you did not use the  
2 appropriate proxy for a risk-free rate in your CAPM model?

3 A. No. Despite Dr. Villadsen's assertion, I have used an appropriate  
4 Treasury instrument to calculate the risk premium in my CAPM model for  
5 regulatory purposes. As I have stated in my direct testimony, the life of a  
6 5-year treasury instrument closely matches the three to five year time  
7 frame in which utilities, such as AAWC, apply for rates.

8  
9 Q. Please address Dr. Villadsen's argument regarding your reliance on  
10 geometric means in your CAPM analyses.

11 A. As I stated in my direct testimony there is an on-going debate over which  
12 is the better average to rely on. However, it is important to recognize that  
13 the information on both means, published by Morningstar, is widely  
14 available to the investment community. For this reason alone I believe  
15 that the use of both means in a CAPM analysis is appropriate.

16  
17 Q. Has the Commission authorized rates of return that were derived through  
18 the use of both arithmetic and geometric means in prior decisions?

19 A. Yes, a case that specifically comes to mind involved UNS Gas Inc., in  
20 which Decision No. 70011, dated November 27, 2007, stated the  
21 following:

22 "We agree with the Staff and RUCO witnesses that it is appropriate  
23 to consider the geometric returns in calculating a comparable  
24 company CAPM because to do otherwise would fail to give  
25

1 recognition to the fact that many investors have access to such  
2 information for purposes of making investment decisions."  
3

4 In the UNS Gas, Inc. case, the ACC Staff witness was Mr. David C.  
5 Parcell who, as I do, consistently relies on both arithmetic and geometric  
6 means in our CAPM analyses. Also, when he testified in the Arizona  
7 Water case, Mr. Parcell, Staff's expert, acknowledged that he uses both  
8 geometric and arithmetic means in his testimony and did so in this case.<sup>4</sup>  
9 Mr. Parcell further testified that Value Line calculates both historic and  
10 prospective growth rates on a geometric or compound growth rate basis.<sup>5</sup>  
11 He further testified that because investors, the Securities & Exchange  
12 Commission and this Commission use arithmetic and geometric means,  
13 analysts developing cost of capital should too.<sup>6</sup>  
14

15 Q. Please respond further to Dr. Villadsen's criticism of your reliance on  
16 geometric means in the CAPM model.

17 A. The best argument in favor of the geometric mean is that it provides a  
18 truer picture of the effects of compounding on the value of an investment  
19 when return variability exists. This is particularly relevant in the case of  
20 the return on the stock market, which has had its share of ups and downs  
21 over the 1926 to 2008 observation period used in my CAPM analysis.  
22

---

<sup>4</sup> T: 1345-46

<sup>5</sup> Id.

<sup>6</sup> Id.

1 Q. Can you provide an example to illustrate the differences between the two  
2 averages?

3 A. Yes. The following example may help. Suppose you invest \$100 and  
4 realize a 20.0 percent return over the course of a year. So at the end of  
5 year 1, your original \$100 investment is now worth \$120. Now let's say  
6 that over the course of a second year you are not as fortunate and the  
7 value of your investment falls by 20.0 percent. As a result of this, the  
8 \$120 value of your original \$100 investment falls to \$96. An arithmetic  
9 mean of the return on your investment over the two-year period is zero  
10 percent calculated as follows:

11  
12 
$$(\text{year 1 return} + \text{year 2 return}) \div \text{number of periods} =$$

13 
$$(20.0\% + -20.0\%) \div 2 =$$

14 
$$(0.0\%) \div 2 = \underline{0.0\%}$$

15  
16 The arithmetic mean calculated above would lead you to believe that you  
17 didn't gain or lose anything over the two-year investment period and that  
18 your original \$100 investment is still worth \$100. But in reality, your  
19 original \$100 investment is only worth \$96. A geometric mean on the  
20 other hand calculates a compound return of negative 2.02 percent as  
21 follows:

22  
23 
$$(\text{year 2 value} \div \text{original value})^{1/\text{number of periods}} - 1 =$$



1                                     $( \$96 \div \$100 )^{1/2} - 1 =$

2                                     $( 0.96 )^{1/2} - 1 =$

3                                     $( 0.9798 ) - 1 =$

4                                     $-0.0202 = \underline{-2.02\%}$

5  
6            The geometric mean calculation illustrated above provides a truer picture  
7            of what happened to your original \$100 over the two-year investment  
8            period.

9            As can be seen in the preceding example, in a situation where return  
10           variability exists, a geometric mean will always be lower than an arithmetic  
11           mean, which probably explains why utility consultants typically put up a  
12           strenuous argument against the use of a geometric mean.

13  
14    Q.    Can you cite any other evidence that supports your use of both a  
15           geometric and an arithmetic mean?

16    A.    Yes. In the third edition of their book, Valuation: Measuring and Managing  
17           the Value of Companies, authors Tom Copeland, Tim Koller and Jack  
18           Murrin ("CKM") make the point that, while the arithmetic mean has been  
19           regarded as being more forward-looking in determining market risk  
20           premiums, a true market risk premium may lie somewhere between the  
21           arithmetic and geometric averages published in Morningstar's SBBI  
22           yearbook.

1 Q. Please explain.

2 A. In order to believe that the results produced by the arithmetic mean are  
3 appropriate, you have to believe that each return possibility included in the  
4 calculation is an independent draw. However, research conducted by  
5 CKM demonstrates that year-to-year returns are not independent and are  
6 actually auto correlated (i.e. a relationship that exists between two or more  
7 returns, such that when one return changes, the other, or others, also  
8 change), meaning that the arithmetic mean has less credence. CKM also  
9 explains two other factors that would make the Morningstar arithmetic  
10 mean too high. The first factor deals with the holding period. The  
11 arithmetic mean depends on the length of the holding period and there is  
12 no "law" that says that holding periods of one year are the "correct"  
13 measure. When longer periods (e.g. 2 years, 3 years etc.) are observed,  
14 the arithmetic mean drops about 100 basis points. The second factor  
15 deals with a situation known as survivor bias. According to CKM, this is a  
16 well-documented problem with the Morningstar historical return series in  
17 that it only measures the returns of successful firms. That is, those firms  
18 that are listed on stock exchanges. The Morningstar historical return  
19 series does not measure the failures, of which there are many. Therefore,  
20 the return expectations in the future are likely to be lower than the  
21 Morningstar historical averages. After conducting their analysis, CKM  
22 conclude that 4.0 percent to 5.5 percent is a reasonable forward-looking  
23 market risk premium. Adding my 2.43 percent risk free yield on a 5-year

1 Treasury instrument to these two estimates indicates a cost of equity of  
2 6.43 percent to 7.93 percent. My recommended cost of equity of 9.50  
3 percent falls above. Given the fact that utilities generally exhibit less risk  
4 than industrials, a return in the low end of this range could be considered  
5 reasonable. My recommended cost of common equity of 9.50 percent is  
6 305 basis points higher the low end of the range.

7

8 Q. Does your silence on any of the issues or positions addressed in the  
9 rebuttal testimony of Mr. Broderick, Dr. Villadsen or any of the Company's  
10 other witnesses constitute acceptance?

11 A. No, it does not.

12

13 Q. Does this conclude your surrebuttal testimony?

14 A. Yes, it does.

# **ATTACHMENT A**

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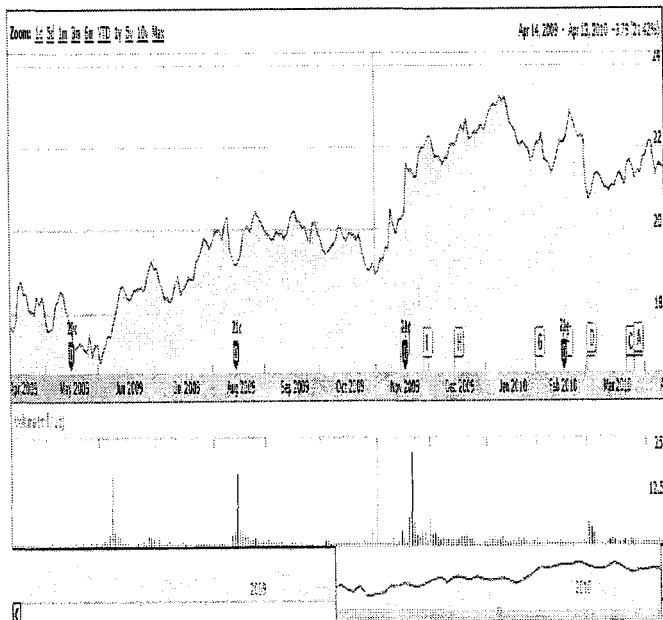
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 Range 21  
 52 week 16  
 Open  
 Vol / Avg. 595,097

<u>Dow</u>	11,019.42	0.12%
<u>S&amp;P 500</u>	1,197.30	0.07%
<u>Utilities</u>		-0.29%
<b>AWK</b>	21.48	-0.32%

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## Key stats and ratios

	Q4 (Dec '09)	2009
Net profit margin	6.08%	-9.55%
Operating margin	22.98%	7.11%

				Val
	<u>Company name</u>	<u>Price</u>	<u>Change</u>	<u>Chg</u>
<b>AWK</b>	<b><u>American Water Works C...</u></b>	21.48	-0.07	-0.3%
<b>SWWC</b>	<b><u>SouthWest Water Company</u></b>	10.48	0.00	0.0%
<b>WTR</b>	<b><u>Aqua America, Inc.</u></b>	17.97	+0.09	0.5%
<b>AWR</b>	<b><u>American States Water Co.</u></b>	37.04	0.00	0.0%
<b>CWT</b>	<b><u>California Water Servi...</u></b>	38.51	+0.52	1.3%
<b>ARTNA</b>	<b><u>Artesian Resources Corp.</u></b>	17.67	+0.04	0.2%
<b>SJW</b>	<b><u>SJW Corp.</u></b>	27.27	+0.41	1.5%
<b>MSEX</b>	<b><u>Middlesex Water Company</u></b>	17.44	+0.15	0.8%
<b>CTWS</b>	<b><u>Connecticut Water Serv...</u></b>	23.15	+0.20	0.8%
<b>YORW</b>	<b><u>The York Water Company</u></b>	13.96	+0.13	0.9%
<b>CDZI</b>	<b><u>Cadiz Inc.</u></b>	12.53	+0.09	0.7%

Sector: [Utilities](#) > Industry: [Water Utilities](#)

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### Description

American Water Works Company, Inc. is a water and wastewater utility company. The Company provides approximately 16 million people with drinking water, wastewater and other water-related services in 35 states and two Canadian provinces. It operates in two segments: Regulated Businesses and Non-Regulated Businesses segments. During the year ended December 31, 2009, the Company's Regulated Businesses accounted for 90.4% of its total operating revenue. During 2009, its Non-Regulated Businesses accounted for 10.6% of the Company's total operating revenue. In December 2009, the Company acquired Environmental Management Corporation (EMC). During 2009, the Company closed on seven acquisitions (six regulated water and wastewater systems, and one in its non-regulated segment).

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### Officers and directors

<a href="#">George MacKenzie</a>	Chairman of the Board
<a href="#">Donald L. Correll</a>	President, Chief Executive Officer, Director
<a href="#">Ellen C. Wolf</a>	Chief Financial Officer, Senior Vice President
<a href="#">Walter J. Lynch</a>	President, Chief Operating Officer - Regulated Operations
<a href="#">Mark F. Strauss</a>	President of American Water Enterprises
<a href="#">Kathy L. Pape</a>	President, Pennsylvania American Water
<a href="#">John R.</a>	President, New Jersey American Water

EBITD margin	-	17.88%
Return on average assets	1.09%	-1.75%
Return on average equity	3.65%	-5.75%
Employees	7,700	-
Carbon Disclosure Rating	-	-

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### Address

1025 Laurel Oak Road  
Voorhees, NJ 08043  
United States - [Map](#)  
+1-856-3468200 (Phone)  
+1-856-3468360 (Fax)

### Website links

Company website:  
<http://www.amwater.com>

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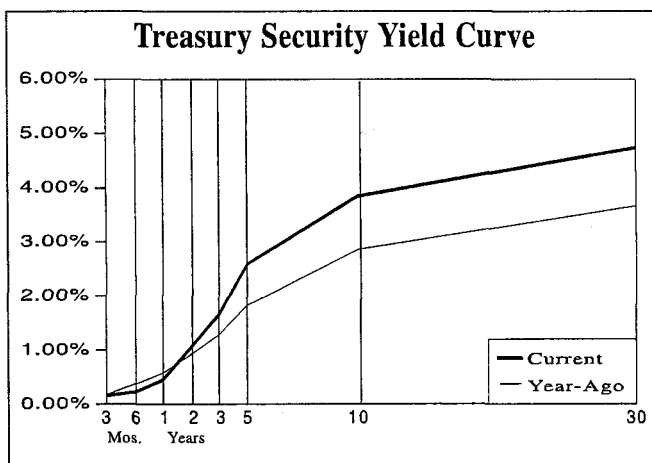
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## **ATTACHMENT B**



## Selected Yields

	Recent (4/07/10)	3 Months Ago (1/06/10)	Year Ago (4/08/09)		Recent (4/07/10)	3 Months Ago (1/06/10)	Year Ago (4/08/09)
TAXABLE							
Market Rates				Mortgage-Backed Securities			
Discount Rate	0.75	0.50	0.50	GNMA 6.5%	2.66	3.70	3.40
Federal Funds	0.00-0.25	0.00-0.25	0.00-0.25	FHLMC 6.5% (Gold)	1.96	2.72	2.79
Prime Rate	3.25	3.25	3.25	FNMA 6.5%	2.25	2.81	2.79
30-day CP (A1/P1)	0.18	0.14	0.33	FNMA ARM	2.76	3.24	3.15
3-month LIBOR	0.30	0.25	1.14	Corporate Bonds			
Bank CDs				Financial (10-year) A	5.24	5.60	7.85
6-month	0.25	0.29	0.83	Industrial (25/30-year) A	5.76	5.83	6.27
1-year	0.44	0.54	1.04	Utility (25/30-year) A	5.91	5.86	6.20
5-year	1.99	2.02	2.05	Utility (25/30-year) Baa/BBB	6.35	6.50	7.63
U.S. Treasury Securities				Foreign Bonds (10-Year)			
3-month	0.16	0.05	0.18	Canada	3.63	3.62	2.90
6-month	0.23	0.14	0.37	Germany	3.12	3.38	3.21
1-year	0.45	0.36	0.58	Japan	1.41	1.34	1.46
5-year	2.60	2.59	1.83	United Kingdom	4.06	4.05	3.35
10-year	3.85	3.82	2.86	Preferred Stocks			
10-year (inflation-protected)	1.52	1.37	1.53	Utility A	6.00	5.94	6.35
30-year	4.74	4.69	3.67	Financial A	6.63	6.80	7.80
30-year Zero	5.00	4.88	3.67	Financial Adjustable A	5.48	5.48	5.48



### TAX-EXEMPT

Bond Buyer Indexes			
20-Bond Index (GOs)	4.44	4.25	4.95
25-Bond Index (Revs)	4.94	4.95	5.75
General Obligation Bonds (GOs)			
1-year Aaa	0.38	0.28	0.47
1-year A	1.18	1.25	1.20
5-year Aaa	1.86	1.68	2.03
5-year A	2.81	2.79	3.45
10-year Aaa	3.31	3.29	3.20
10-year A	4.29	4.20	4.75
25/30-year Aaa	4.46	4.47	4.77
25/30-year A	5.51	5.41	6.25
Revenue Bonds (Revs) (25/30-Year)			
Education AA	4.78	4.83	6.30
Electric AA	4.79	4.74	6.40
Housing AA	5.73	5.76	6.70
Hospital AA	5.19	5.04	6.65
Toll Road Aaa	4.78	4.80	6.45

## Federal Reserve Data

### BANK RESERVES

(Two-Week Period; in Millions, Not Seasonally Adjusted)

	Recent Levels			Average Levels Over the Last...		
	3/24/10	3/10/10	Change	12 Wks.	26 Wks.	52 Wks.
Excess Reserves	1103635	1163154	-59519	1100918	1055784	925591
Borrowed Reserves	88326	101275	-12949	124739	184163	314469
Net Free/Borrowed Reserves	1015309	1061879	-46570	976179	871620	611121

### MONEY SUPPLY

(One-Week Period; in Billions, Seasonally Adjusted)

	Recent Levels			Growth Rates Over the Last...		
	3/22/10	3/15/10	Change	3 Mos.	6 Mos.	12 Mos.
M1 (Currency+demand deposits)	1716.1	1708.2	7.9	4.9%	7.3%	9.9%
M2 (M1+savings+small time deposits)	8480.1	8490.1	-10.0	-2.4%	0.4%	0.9%

**ARIZONA-AMERICAN WATER COMPANY**

**DOCKET NO. W-01303A-09-0343  
AND DOCKET NO. SW-01303A-09-0343**

**SURREBUTTAL TESTIMONY**

**OF**

**RALPH C. SMITH**

**ON BEHALF OF**

**THE**

**RESIDENTIAL UTILITY CONSUMER OFFICE**

**APRIL 15, 2010**

BEFORE THE ARIZONA CORPORATION COMMISSION

KRISTIN K. MAYES  
Chairman  
GARY PIERCE  
Commissioner  
PAUL NEWMAN  
Commissioner  
SANDRA D. KENNEDY  
Commissioner  
BOB STUMP  
Commissioner

---

IN THE MATTER OF THE APPLICATION OF )  
ARIZONA-AMERICAN WATER COMPANY, AN ) DOCKET NO. W-01303A-09-0343  
ARIZONA CORPORATION, FOR A DETERMINATION )  
OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT )  
AND PROPERTY AND FOR INCREASES IN ITS RATES )  
AND CHARGES BASED THEREON FOR UTILITY )  
SERVICE BY ITS ANTHEM WATER DISTRICT AND ITS )  
SUN CITY WATER DISTRICT )

---

IN THE MATTER OF THE APPLICATION OF )  
ARIZONA-AMERICAN WATER COMPANY, AN ) DOCKET NO. SW-01303A-09-0343  
ARIZONA CORPORATION, FOR A DETERMINATION )  
OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT )  
AND PROPERTY AND FOR INCREASES IN ITS RATES )  
AND CHARGES BASED THEREON FOR UTILITY )  
SERVICE BY ITS ANTHEM/AGUA FRIA WASTEWATER )  
DISTRICT, ITS SUN CITY WASTEWATER DISTRICT )  
AND ITS SUN CITY WEST WASTEWATER DISTRICT )

SURREBUTTAL  
TESTIMONY  
OF  
RALPH C. SMITH  
ON BEHALF OF THE  
RESIDENTIAL UTILITY CONSUMER OFFICE  
APRIL 15, 2010

## TABLE OF CONTENTS

	<u>Page</u>
I. INTRODUCTION .....	1
II. REVENUE REQUIREMENT .....	1
III. RATE BASE .....	4
Plant Adjustments .....	5
B-1 Post Test Year Plant – Sun City Water .....	6
B-2 Agua Fria Wastewater – Retirement of Two Effluent Pumps .....	9
B-3 CIAC in CWIP (All Districts Except Sun City West Wastewater) .....	9
B-4 Cash Working Capital (All Districts) .....	10
1. Revenue Lag .....	11
2. Service Company Payment Lag .....	22
3. Other Expense Adjustments .....	31
4. Remove Chemical Expense .....	32
5. Remove Uncollectibles .....	32
B-5 Youngtown Plant – Sun City Water .....	33
B-6 Verrado Wastewater Plant – Anthem/Agua Fria Wastewater .....	34
B-7 Comprehensive Planning Study – Sun City and Sun City West Wastewater .....	35
B-8 North West Valley Treatment Plant – Anthem/Agua Fria and Sun City West Wastewater .....	36
B-9 Accumulated Deferred Income Taxes .....	37
Other Rate Base Adjustments .....	39
IV. ADJUSTMENTS TO OPERATING INCOME .....	40
C-1 Customer Annualization Correction (Anthem Water District) .....	41
C-2 Rate Case Expense (All Districts) .....	41
C-3 Incentive Compensation Expense – AAWC Employees (All Districts) .....	47
C-4 Stock-Based Compensation Expense (All Districts) .....	58
C-5 Normalized Pension Expense (All Districts) .....	60
Company’s Request to Defer Pension Expense .....	78
Company’s Request to Charge Ratepayers for an Amortization of a Pension “Regulatory Asset” .....	79
C-6 Normalized Other Post Employment Benefits Expense (All Districts) .....	81
C-7 Donations, Membership Dues, Advertising and Miscellaneous (All Districts) .....	83
C-8 Tank Maintenance Reserve Fund Accrual (Sun City Water and Anthem Water) .....	83
1. Sun City Water Tank Maintenance Reserve Fund Accrual .....	85
2. Anthem Water Tank Maintenance Reserve Fund Accrual .....	88
C-9 Affiliate Management Fees – Remove 4% Increase to “Other Expense” .....	91
C-9A Affiliate Management Fees – Remove 4% March 2009 Pay Increase .....	92
C-10 Affiliate Management Fees – Remove 22.22% Post Test Year Increase for Affiliate Employee Benefits .....	93
C-11 Affiliate Management Fees – Remove Affiliate Incentive Compensation Expense .....	96
C-12 Affiliate Management Fees – Normalize Affiliate Pension Expense .....	98
C-13 Affiliate Management Fees – Normalize Affiliate OPEB Expense .....	99
C-14 Affiliate Management Fees – Remove Affiliate “Business Development” Costs .....	100
C-15 Interest Synchronization (All Districts) .....	101
C-16 Depreciation Expense (Sun City Water) .....	101
C-17 Depreciation Expense (Agua Fria Wastewater) .....	102
C-18 Depreciation Expense (Anthem Water) .....	102
C-19 Depreciation Expense (Anthem/Agua Fria Wastewater) .....	102
Other Expense Adjustments .....	103
V. AAWC’S REBUTTAL FILING REQUEST FOR A MAJOR NEW ACCOUNTING DEFERRAL .....	103

**ATTACHMENTS**

Updated RUCO Accounting Schedules- Water Districts .....RCS-6

Updated RUCO Accounting Schedules- Wastewater Districts .....RCS-7

Non-confidential material referenced in surrebuttal testimony and schedules .....RCS-8

1     **I.     INTRODUCTION**

2     **Q.     Please state your name, position and business address.**

3     A.     Ralph C. Smith. I am a Senior Regulatory Consultant at Larkin & Associates, PLLC,  
4             15728 Farmington Road, Livonia, Michigan 48154.

5  
6     **Q.     Are you the same Ralph C Smith who previously filed direct testimony in this**  
7             **proceeding?**

8     A.     Yes. I previously filed direct testimony on behalf of the Residential Utility Consumer  
9             Office ("RUCO").

10  
11    **Q.     What is the purpose of the surrebuttal testimony you are presenting?**

12    A.     The purpose of my surrebuttal testimony is to respond to the rate base, adjusted net  
13             operating income and revenue requirement issues addressed in the rebuttal testimony filed  
14             by Arizona-American Water Company ("Arizona-American", "AAWC," or "Company").

15  
16    **Q.     Have you prepared any exhibits to be filed with your testimony?**

17    A.     Yes. Attachments RCS-6 through RCS-8 contain the results of my analysis and copies of  
18             selected documents that are referenced in my testimony, respectively.

19  
20    **II.    REVENUE REQUIREMENT**

21    **Q.     What issues are addressed in your surrebuttal testimony?**

22    A.     My testimony addresses the Company's proposed revenue requirement and selected other  
23             issues.

**Q. What revenue increase was originally requested by AAWC?**

A. For the districts included in its current filing, AAWC is requesting an increase in base rate revenues of \$20.498 million, or approximately 56 percent over adjusted revenues at current rates as shown in the following table:

Summary of Requested Rate Increases per Company in its Direct Filing

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjusted TY Rate Base	\$ 7,268,177	\$2,531,127	\$7,060,837	\$2,156,882	\$ 1,480,756	\$ 20,497,779
Adjusted Current Revenues	\$ 7,210,624	\$9,125,203	\$8,634,567	\$5,933,970	\$ 5,660,389	\$ 36,564,753
% Change	100.80%	27.74%	81.77%	36.35%	26.16%	56.06%

The requested revenue amount is from Company Schedule A in AAWC's filing and is also shown on RUCO Schedule A on Attachments RCS-6 and RCS-7.

**Q. Has AAWC revised its proposed revenue increase in its rebuttal filing?**

A. Yes. AAWC witness Broderick's rebuttal testimony at page 1, indicates that AAWC is now seeking a total revenue increase of \$16.583 million or 44.8<sup>1</sup> percent. Page 4 of his rebuttal lists the increased revenue that AAWC is now seeking for each district. In its rebuttal testimony, AAWC adopted some Staff and RUCO recommendations. AAWC's rebuttal reflects the following company-requested revenue increases.

<sup>1</sup> The combined percentage increase does not calculate exactly to the summary table shown below.

Summary of Requested Rate Increases per Company - Per Rebuttal

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjusted TY Rate Base	\$ 5,962,687	\$ 2,026,980	\$ 5,308,323	\$ 1,858,070	\$ 1,426,944	\$16,583,004
Adjusted Current Revenues	\$ 7,220,094	\$ 9,125,203	\$ 8,634,509	\$ 5,934,616	\$ 5,660,389	\$36,574,811
% Change	82.58%	22.21%	61.48%	31.31%	25.21%	45.34%

**Q. What revenue increase does RUCO recommend?**

**A.** RUCO recommends a revenue increase on adjusted fair value rate base, for each AAWC division, of no more than the amounts listed in the following table:

Summary of RUCO Recommended Rate Increases By District

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjusted TY Rate Base	\$ 5,296,426	\$ 682,709	\$5,085,007	\$1,513,691	\$ 783,855	\$ 13,361,688
Adjusted Current Revenues	\$ 7,220,082	\$9,125,203	\$8,634,567	\$5,933,970	\$ 5,660,389	\$ 36,574,211
% Change	73.36%	7.48%	58.89%	25.51%	13.85%	36.53%

Details of how these amounts of revenue deficiency were derived are shown in Attachments RCS-6 and RCS-7 to my surrebuttal testimony. The revenue deficiency for each water district is presented in Attachment RCS-6 on the respective "Schedule A" for that district. A "Schedule A" has also been presented for the total water districts and, separately, the total wastewater districts, for which rate increases have been sought by AAWC in the current rate case. Attachment RCS-7 presents similar information for each wastewater district.



1

2 **Q. How have you designated the districts on Attachments RCS-6 and RCS-7?**

3 A. I have used the following designations for the districts on Attachment RCS-6:

4 “(A)” for Anthem Water

5 “(SC)” for Sun City Water

6 I have used the following designations for the districts on Attachment RCS-7:

7 “(AAF)” for Anthem/Agua Fria Wastewater

8 “(SC)” for Sun City Wastewater

9 “(SCW)” for Sun City West Wastewater

10 These are the same district designations used in Attachments RCS-2 and RCS-3,  
11 respectively, which were filed with my direct testimony.

12

13 **III. RATE BASE**

14 **Q. Have you prepared updated schedules that summarize RUCO’s proposed**  
15 **adjustments to rate base?**

16 A. Yes. As noted above, in Attachments RCS-6 and RCS-7, respectively, for each district,  
17 and in summary for the water systems and, separately, for the wastewater districts  
18 included in AAWC’s filing, I have prepared an updated Schedule B, which shows the rate  
19 base originally requested by AAWC, RUCO’s updated adjustment and RUCO’s adjusted  
20 rate base. The adjustments to AAWC’s proposed rate base are shown on Schedule B.1. A  
21 comparison of the Company’s proposed rate base and RUCO’s recommended rate base,  
22 by district, is presented below:

### Rate Base Summary - Water and Wastewater Districts

District	Per Company		
	As-Filed	Per RUCO	Difference
Anthem Water	\$ 57,430,025	\$ 57,259,174	\$ (170,851)
Sun City Water	\$ 28,186,063	\$ 26,215,284	\$ (1,970,779)
Subtotal -Water	\$ 85,616,088	\$ 83,474,458	\$ (2,141,630)
 Anthem/Agua Fria Wastewater	 \$ 47,735,732	 \$ 45,264,942	 \$ (2,470,790)
Sun City Wastewater	\$ 14,764,087	\$ 14,596,027	\$ (168,060)
Sun City West Wastewater	\$ 17,821,272	\$ 18,098,016	\$ 276,744
Subtotal -Wastewater	\$ 80,321,091	\$ 77,958,985	\$ (2,362,106)
 Total Rate Base	 \$ 165,937,179	 \$ 161,433,443	 \$ (4,503,736)

### Plant Adjustments

**Q. What response did AAWC provide in its rebuttal to the two adjustments to AAWC's requested plant in service that you had recommended in your direct testimony?**

**A.** AAWC disagreed with my first adjustment, B-1, which affects only the Sun City Water district, and removes an item of post-test year plant that AAWC had requested.<sup>2</sup> The Company agreed with my second adjustment, B-2, which affects only the Agua Fria Wastewater district, and removes the cost of two effluent pumps that had been retired during the test year.<sup>3</sup>

**Q. In its rebuttal did AAWC also adopt a number of adjustments to Plant in rate base that Staff had recommended?**

**A.** Yes.

<sup>2</sup> See, e.g., Broderick rebuttal at pages 8-9; Gross rebuttal at pages 1-2.

<sup>3</sup> See, e.g., Murrey rebuttal.

**B-1 Post Test Year Plant – Sun City Water**

**Q. Please explain why the Company's request to include in the Sun City Water rate base plant that was not in service during the test year should be rejected.**

A. The Company has proposed to include in rate base the cost for a new well that was placed into service on May 27, 2009, at an amount of \$1.587 million. This amount should be removed because it was not in service during the test year and because AAWC has failed to demonstrate special or unusual circumstances to justify inclusion of the post test year plant additions in rate base.

**Q. Please elaborate on why post test year plant should be removed in the current AAWC rate case.**

A. The test year is the one-year historical period used in determining rate base, operating income and rate of return. Commission's rules at A.A.C. R14-2-103(A)(3)(p) require the end of the test year to be the most recent practical date available prior to the filing. A utility has the freedom to choose a test year that includes all major rate base and operating income items needed to support its rate application, and to include pro forma adjustments to its test year. The "matching" concept is a fundamental principle of accounting and ratemaking. The absence of matching distorts the coordination the elements of the ratemaking formula, and can adversely affect the fairness and reasonableness of rates. My understanding is that the Commission has only allowed inclusion of post test year plant in special and unusual circumstances that warranted such recognition. Decision No. 71410, at page 20, cites the following two types of situations that have warranted rate base recognition of post-test year plant:

1                   (1) when the magnitude of the investment relative to the utility's total investment is  
2                   such that not including the post test year plant in the cost of service would  
3                   jeopardize the utility's financial health; and

4                   (2) when certain conditions exist as follows:

5                   (a) the cost of the post test year plant is significant and substantial;

6                   (b) the net impact on revenue and expenses for the post test year plant is known  
7                   and insignificant or is revenue-neutral; and

8                   (c) the post test year plant is prudent and necessary for the provision of services  
9                   and reflects appropriate, efficient, effective, and timely decision-making.

10                  In the current rate case, AAWC has not demonstrated special or unusual circumstances to  
11                  justify inclusion of the post test year plant additions in rate base. The \$1.587 million is  
12                  not of such magnitude to AAWC such that not including it would jeopardize the utility's  
13                  financial health. As a portion of AAWC plant of the districts included in the current  
14                  filing, the \$1.587 million is approximately 1.06 percent of the Gross Utility Plant in  
15                  Service of \$149,301,020 that AAWC proposed in its initial filing for the water districts,  
16                  and is only 0.47 percent of the combined total water and wastewater Gross Utility Plant in  
17                  Service in AAWC's filing, as shown in the following table:

**Sun City Well No. 5.1 As Percent of Total Plant in Service  
For AAWC Districts Included in the Current Rate Case**

<u>Description</u>	<u>Amount</u>	<u>Item</u>
Gross Utility Plant in Service		
Water Districts in the Current AAWC Case	\$ 149,301,020	A
Wastewater Districts in the Current AAWC Case	\$ 191,762,219	
Combined Gross Utility Plant in Service	<u>\$ 341,063,239</u>	B
AAWC Proposed Post-Test Year Additions to Plant - Well 5.1 - Sun City Water	<u>\$ 1,587,149</u>	C
Percent of Combined Water Plant	<u>1.06%</u>	C/A
Percent of Combined Water and Sewer Plant	<u>0.47%</u>	C/B
<u>Notes and Source</u>		
AAWC Filing, Schedule B-1		

The districts in the current AAWC rate filing only represent a portion of AAWC's total investment in Gross Utility Plant in Service, so the percent of the AAWC total company amount represented by the \$1.587 million post-test year plant item is even smaller.

**Q. Was a similar AAWC-proposed adjustment for post test year plant rejected by the Commission in AAWC's last rate case?**

A. Yes. In AAWC's last rate case, for reasons similar to those stated above, in Decision No. 71410 for Agua Fria Water, Mohave Water and Mohave Wastewater, the Commission removed AAWC's request for post test year plant.

**Q. What adjustment is needed?**

A. This adjustment is shown on Attachment RCS-6, Schedule B-1, and reduces rate base by \$1.587 million to remove post-test year plant for the Sun City Water district.

1  
2 **Q. Is there a related adjustment to expense?**

3 A. Yes. As shown on Attachment RCS-6, Schedule C-16, Arizona-American's proposed  
4 depreciation expense for Sun City Water is reduced by \$36,961 based on applying the  
5 applicable depreciation rates to the plant adjustment. I discuss this related adjustment to  
6 depreciation expense in a subsequent section of my testimony.  
7

8 **B-2 Agua Fria Wastewater – Retirement of Two Effluent Pumps**

9 **Q. Has AAWC accepted your recommended adjustment of plant in service for the Agua**  
10 **Fria Wastewater for the Retirement of Two Effluent Pumps?**

11 A. Yes, as indicated in AAWC witness Murrey's rebuttal testimony at page 6.  
12

13 **B-3 CIAC in CWIP (All Districts Except Sun City West Wastewater)**

14 **Q. Has AAWC accepted your recommended adjustment relating to CIAC in CWIP?**

15 A. Yes. Initially, the Company contended that Contributions in Aid of Construction  
16 ("CIAC") associated with Construction Work in Progress ("CWIP") should not be  
17 deducted from rate base, because there is no offsetting plant in rate base. RUCO and Staff  
18 made adjustments to reflect the full amount of CIAC as a deduction from rate base. This  
19 is necessary and appropriate because it is the Company's choice whether to accept plant or  
20 funds from developers, and if the Company chooses to accept plant, then the Company is  
21 not expending funds for the plant and thus has funds for other uses. Additionally, the  
22 Company's position is contrary to traditional ratemaking practices and contrary to the  
23 National Association of Regulatory Utility Commissioners ("NARUC") definition of

CIAC, which does not distinguish between CIAC associated with CWIP and CIAC associated with plant in service. AAWC witness Murrey's rebuttal testimony at pages 5- 7 indicates that AAWC has accepted the Staff and RUCO adjustments "because the amounts are immaterial and the Company has improved its accounting for developer projects to eliminate this inconsistency in the future." However, this adjustment should be adopted for the reasons stated in my direct testimony and in Decision No. 71410 where the Commission stated at pages 27-28 that:

We agree with RUCO and Staff that the Company's choice whether to accept plant or funds from developers is irrelevant, and does not change the nature of AIAC or CIAC. The evidence in this case does not persuade us to depart from the traditional ratemaking treatment of deducting AIAC and CIAC from rate base. The adjustments recommended by RUCO and Staff will be adopted.

**Q. What adjustment is necessary in the current AAWC rate case?**

**A.** As shown on Attachment RCS-6, Schedule B-3, rate base should be reduced by \$138,495 in total, and by the amounts shown there, and listed below for each district:

Summary of Adjustments to CIAC

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (30,271)	\$ (38,991)	\$ (65,490)	\$ (3,743)	\$ -	\$ (138,495)

**B-4 Cash Working Capital (All Districts)**

**Q.** What cash working capital ("CWC") issues do you address in your surrebuttal testimony?

A. I respond to AAWC's rebuttal testimony on the revenue lag and affiliated payment issues. I also have adopted certain adjustments that were recommended by Staff to which AAWC has agreed in its rebuttal. Finally, I have updated the CWC calculation to reflect revisions to expenses.

**1. Revenue Lag**

**Q. What is the function of a revenue lag in a lead/lag study?**

A. The revenue lag is supposed to measure, on average, the time between (a) the provision of service and (b) the receipt of payment for service. It typically is comprised of three sub-component lags: (1) the service period lag, (2) the billing lag, and (3) the collection lag.

**Q. What revenue lags did AAWC use in its lead/lag study?**

A. The revenue lags used by AAWC for each district is summarized in the table below:

Summary of Revenue Lag as calculated by AAWC					
Revenue Lag Component	Anthem Water	Sun City Water	Anthem Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater
Service Period Lag	15.148	15.219	15.248	15.335	15.394
Billing Lag	4.875	4.426	4.711	4.317	4.216
Collection Lag	26.082	26.082	26.082	26.091	26.018
<b>Total Revenue Lag Days</b>	<b>46.105</b>	<b>45.727</b>	<b>46.040</b>	<b>45.743</b>	<b>45.628</b>

The Company's lead lag study uses a collection lag, by service area, ranging from 26.018 days to 26.091 days. This effectively assumes that customers, on average, throughout the year, are not complying with the payment terms. The payment terms are supposed to be reflected in the dates printed on the customers' bills and with the terms of AAWC's tariff. As discussed in more detail below, the due date for payment of billings for water and wastewater service is 20 days and does not differ by the type of customer.



1  
2 **Q. Please identify the components of the Revenue Lag proposed by AAWC and which of**  
3 **those components indicate inefficiency?**

4 A. The Revenue Lag is comprised of these three components: (1) Service Period; (2) Billing  
5 Lag; and (3) Collection Lag. AAWC's Service Period lag of approximately 15.2 days is  
6 comparable to other utilities that bill customers monthly, and I am not taking issue with  
7 the Company's Service Period lag.

8 However, the components of the Revenue Lag proposed by AAWC that indicate  
9 inefficiency are the Billing Lag and the Collection Lag. An adjustment needs to be made  
10 to AAWC's total proposed Revenue Lag to address this, otherwise ratepayers would be  
11 required to pay an extra return on rate base caused by inefficiency in billing and  
12 collection.

13 The total proposed Revenue Lag proposed by AAWC is longer than for other  
14 Arizona utilities that use monthly billing and which have utilized lead-lag studies.

15  
16 **Q. How does the Company attempt to justify its total revenue lags that exceed 45 days**  
17 **for each district?**

18 A. AAWC witness Gutowski bases AAWC's justification for the long revenue lags proposed  
19 by the Company on the following:

- 20 • The Commission has accepted the Company's calculation of Revenue Lag in prior  
21 cases without question.<sup>4</sup>  
22 • Charge offs have increased.<sup>5</sup>

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<sup>4</sup> Gutowski rebuttal, page 8, lines 17-18.

- 1           • For the Collection Lag, AAWC divided Accounts Receivable Balances per day by
- 2           365 days.<sup>6</sup>
- 3           • The Company has a late payment fee, “[b]ut the late payment penalty was never
- 4           designed to be a money maker, or to compensate the Company for the delayed
- 5           receipt of revenue.”<sup>7</sup>
- 6           • The Commission should ignore the more efficient (shorter) Billing Lag period used
- 7           by other Arizona utilities, and should accept AAWC’s lag because it was
- 8           calculated the same way it always has been, billing date minus read date.<sup>8</sup>

9

10   **Q.    Should the fact that the Commission accepted something a utility did in a prior case**  
11   **that was not questioned require that things must be done the same way, if**  
12   **comparative information demonstrates that a utility is inefficient and the extra costs**  
13   **to ratepayers resulting from the comparative inefficiency are currently being**  
14   **questioned?**

15   **A.    I would hope not. Apparently, AAWC has gotten away with using an excessively long**  
16   **Revenue Lag in prior rate cases, and that may not have been questioned. Usually there are**  
17   **many issues in a utility rate case, and every aspect of a utility’s filing, including ones that**  
18   **cause extra costs to be unnecessarily charged to ratepayers, are not always challenged in**  
19   **every case. It is basically by looking at utility lead-lag study detail in a series of recent**  
20   **Arizona utility rate cases, involving utilities that bill their customers monthly, that the**  
21   **inefficiently long Revenue Lag proposed by AAWC in the current case, came to my**

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<sup>5</sup> Id, lines 22-24.

<sup>6</sup> Gutowski rebuttal, page 9.

<sup>7</sup> Id.

<sup>8</sup> Id.

1 attention. AAWC seems to be saying that it cannot improve its Billing Lag or Collection  
2 Lag, to produce a Revenue Lag that is comparable to what several other Arizona utilities  
3 have achieved. AAWC thus apparently believes that it should be allowed to continue to  
4 include additional amounts of cash working capital in rate base related to its excessive  
5 Revenue Lag and thereby earn higher returns for its investors based on such inefficiency.  
6 AAWC's position thus rewards shareholders and penalizes ratepayers for Company  
7 inefficiency in managing its Revenue Lag, similar to what other Arizona utilities have  
8 achieved.

9  
10 **Q. Why should AAWC's excessive Revenue Lag be adjusted in the current AAWC rate**  
11 **case?**

12 A. I have brought this issue to the Commission's attention in the current AAWC rate case,  
13 and have calculated a recommended remedy that should provide the appropriate regulatory  
14 incentives. By adopting my recommended adjustment to AAWC's Revenue Lag,  
15 ratepayers will no longer be charged for an extra return on rate base caused by AAWC's  
16 inefficiency. Additionally, this should help motivate AAWC to look for ways to improve  
17 its Billing Lag and Collection Lag, to produce a total Revenue Lag that is comparable to  
18 that of the other Arizona utilities that I cited in my direct testimony.

19  
20 **Q. Please respond to Ms. Gutowski's comment that charge offs have increased.**

21 A. Uncollectibles have increased because of the economic downturn, which has made it more  
22 difficult for customers to pay. I am not disputing Ms. Gutowski's representation that  
23 charge-offs have increased. What I am disputing about Ms. Gutowski's position,

1           however, is that this represents a valid reason for failing to adjust Cash Working Capital in  
2           the current AAWC rate case.

3           Uncollectibles should be removed from the Cash Working Capital calculation.  
4           AAWC has agreed with a Staff adjustment to remove Bad Debt Expense from the CWC  
5           calculation. Bad Debt Expense is another term for uncollectibles.

6           The other aspect to Uncollectibles and how it affects Cash Working Capital should  
7           also be adjusted. This other aspect of Uncollectibles relates to how long a Company  
8           carries uncollectible accounts in Accounts Receivable before they are written off or  
9           covered by a reserve for Uncollectibles. Recall that AAWC computed its Revenue Lag by  
10          dividing Accounts Receivable by 365 days to determine Average Daily Accounts  
11          Receivable. Accounts that eventually become uncollectible can distort the Revenue Lag if  
12          they are included in Accounts Receivable for lengthy periods of time without having an  
13          adequate reserve established.

14  
15       **Q. By adjusting the Revenue Lag in the manner in which you have recommended, does**  
16       **that ameliorate this other aspect of Uncollectibles from overstating the CWC**  
17       **allowance?**

18       **A.** Yes. By adjusting the Revenue Lag in the manner in which I have recommended, this  
19       helps ameliorate the impact of including accounts that eventually become uncollectible in  
20       the Accounts Receivable balance that AAWC used to derive its Collection Lag portion of  
21       the Revenue Lag. The cash revenue received by the utility is paid to it by the customers  
22       who pay their bills. Adjusting the Revenue Lag in the manner in which I have  
23       recommended assures that the Revenue Lag is not overstated because of Uncollectibles

1 being carried in Accounts Receivable. It reflects an allowance for the Collection Lag  
2 based on the receipt of cash Revenue from the customers who pay their bills, on average,  
3 by the due date. For customers who pay their utility bills but who do not pay by the due  
4 date, AAWC charges and records late payment fee revenue.

5  
6 **Q. Please respond to Ms. Gutowski's comment that "the late payment penalty was never**  
7 **designed to be a money maker, or to compensate the Company for the delayed**  
8 **receipt of revenue."**

9 **A.** Ms. Gutowski has not presented any evidence of which I am aware which demonstrates  
10 the Company's late payment charge of 1.5 percent is insufficient. Late payment fees are  
11 typically implemented to provide compensation from the cost causative customers for the  
12 Company's financing cost for the cost of money for customers who pay their bills but who  
13 pay late. One of the objectives of late payment fees is to encourage the customers, who  
14 are going to pay their bills, to pay on a timely basis, i.e., to remit payment by the due date  
15 and thereby avoid the late payment fee.

16 If the Company were able to demonstrate that its late payment charges are  
17 insufficient to cover the Company's financing cost for the cost of money for customers  
18 who pay their bills but who pay late (which AAWC has apparently not done in the current  
19 rate case), this would raise a rate design issue. As a rate design issue, it could  
20 appropriately be addressed, if necessary, by revising the level of late payment fee.

21 However, the point with respect to the CWC calculation is that the Company does  
22 have a late payment fee and if the Company believes that it is not covering the appropriate

1 costs, this is not a valid reason for allowing an inefficiently long Revenue Lag and  
2 increasing the rate base for Cash Working Capital.

3  
4 **Q. Why should the Commission consider the information on the Revenue Lags of the**  
5 **Arizona utilities that you presented in your direct testimony?**

6 A. This information should be considered because the other utilities bill customers monthly,  
7 similar to AAWC, and it reflects their achieved level of efficiency in the Billing Lag and  
8 Collection Lag components of the Revenue Lag that should be expected of AAWC. If  
9 AAWC management chooses not to address inefficiencies in its Billing Lag or Collection  
10 Lag that are causing it to have an overall longer Revenue Lag than other Arizona utilities,  
11 the extra cost of that additional lag should be borne by shareholders, not ratepayers.

12  
13 **Q. Are the Revenue Lags used by AAWC appropriate?**

14 A. No. The collection lag period used by AAWC is excessive and would penalize all  
15 customers, including the vast majority of customers that pay their utility bills on time, for  
16 the minority of customers who either pay their bills late or do not pay at all (i.e., whose  
17 bills become uncollectible).

18  
19 **Q. In order to address the impact of accounts that becoming uncollectible on the**  
20 **average Accounts Receivable balances for each district, did you request and did**  
21 **AAWC provide Accounts Receivable aging reports?**

22 A. Such Accounts Receivable aging reports were requested in RUCO 2-74. However,  
23 AAWC's response to RUCO 2-74(j) stated that: "The aging reports are deleted from the

1 system after a short period of time. We are investigating what is required to to (sic)  
2 restore the aging reports by district. The reports are available for the Company as a whole,  
3 but not at the district specific level of detail. If the Company as a whole would suffice,  
4 please let the me (sic) know.”

5  
6 **Q. Without the district aging reports that AAWC could not provide, it is possible to**  
7 **reasonably adjust the collection lag?**

8 A. Yes. A reasonable adjustment to the collection lag can be made by applying the 20 day  
9 due date period as the maximum collection lag that would apply for customers who, on  
10 average, pay their utility bills on time.

11  
12 **Q. Please explain why an adjustment for the revenue collection lag is needed.**

13 A. The Company's lead-lag study uses an unreasonably long revenue lag because its revenue  
14 collection lag extends well beyond the bill payment period. The Company's revenue lag  
15 is also excessive in comparison with other Arizona utilities that bill customers monthly.  
16 For purposes of its lead-lag study, the Company effectively assumes that customers, on  
17 average, are paying their bills late, i.e., are on average not paying their bills by the due  
18 date printed on the bills. Uncollectibles and late payments should be excluded from the  
19 calculation of Cash Working Capital. Before amounts are written-off as uncollectible, the  
20 Company may carry such amounts on its books in Accounts Receivable for several  
21 months, thus distorting the revenue collection lag for customers who, on average, pay their  
22 bills on time. Additionally, bad debt recoveries may be eventually collected several  
23 months after the rendering of the initial bill. Including write-offs and recoveries in the

1 determination of the revenue collection lag, however, can result in a distortion of the time  
2 when normal paying customers pay their bills for the water and sewer utility service. A  
3 more reasonable expectation, and one that excludes the potentially distortive impact of  
4 uncollectibles on the collection lag, is that customers, on average, pay their bills for water  
5 and sewer utility service on or before the due date printed on the bill. Moreover, the  
6 Company charges late fees and receives late fee revenue from the customers who pay their  
7 bills late.

8  
9 **Q. Please explain how you calculated the adjustment for the revenue lag on each**  
10 **respective Schedule B-4, of Attachments RCS-6 and RCS-7.**

11 **A.** I used a maximum period of 20 days for the revenue collection lag for each Arizona  
12 district that AAWC had included in its lead-lag study. This assures that the collection lag  
13 portion of the revenue lag is not overstated in comparison with the terms provided in the  
14 Company's tariff for the payment of the billed revenue. Uncollectibles are removed from  
15 cash working capital because they are a non-cash expense. Before they become  
16 uncollectible, billed revenue amounts may be carried on the company's books as an  
17 account receivable for some time, perhaps even for several months, thus adding to the  
18 revenue collection lag. This necessitates a reasonableness check on the collection lag that  
19 reflects the timely payment of revenues that are collected.

20 As stated in the response to RUCO 2-74(b) and (c), the customer bills issued by  
21 AAWC states when the bill is due, and "due dates are 20 days after the billing date and it  
22 does not differ by type of customer." Moreover, customers are subject to a late charge if



1 payment is made late. As stated in the response to RUCO 2-74(e): "Customers are subject  
2 to a 1-1/2% late charge. It begins by being posted to the account on day 21."

3 For computing the revenue collection lag, I have therefore used the 20 days as the  
4 maximum period, on average, which revenue collection should be occurring, without the  
5 potentially distortive impact of uncollectible write-offs. This adjustment resulted in the  
6 revised revenue lags for each service district as follows:

Adjusted Revenue Lag Days with 20-Day Collection Lag					
Revenue Lag Component	Anthem Water	Sun City Water	Anthem Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater
Service Period Lag	15.148	15.219	15.248	15.335	15.394
Billing Lag	4.875	4.426	4.711	4.317	4.216
Collection Lag	20.000	20.000	20.000	20.000	20.000
Total Revenue Lag Days	40.023	39.645	39.959	39.652	39.610

7  
8  
9 **Q. Why are the Billing Lag days used by AAWC also a concern?**

10 A. The Billing Lag days are supposed to measure the time between the reading of the  
11 customer's meter and the issuance of the bill. With many modern utilities using  
12 automated meter reading and computerized billing software, a Billing Lag exceeding 4  
13 days on average (which is what AAWC is using) also appears to be excessive. The Billing  
14 Lag used by AAWC is therefore also a concern.

15  
16 **Q. Have you calculated a separate adjustment to address the concern with AAWC's  
17 Billing Lag being excessive?**

18 A. No, because adjusting the total Revenue Lag by limiting the Collection Lag to the bill  
19 payment due date, will resolve the overall concern regarding AAWC's proposed revenue

lag, and will provide a total Revenue Lag that is comparable, but at the high end, of the Revenue Lags being used by other large Arizona utilities that bill their customers monthly.

**Q. Please summarize how the revenue lags used by AAWC compare with the revenue lags used in recent rate cases by other large Arizona utilities that bill their customers monthly?**

**A.** The following table summarizes the revenue lags that have been used in several recent rate cases:

Revenue Lag			
Typical Arizona Utilities That Use Monthly Billing			
Utility	Docket	Revenue Lag Days	Reference
APS (Arizona Public Service)	E-01315A-08-0172	38.17	A
TEP (Tucson Electric Power)	E-01933A-07-0402	33.79	B
UNS Gas	G-04204A-08-0571	40.70	C
UNS Electric	E-04204A-09-0206	35.59	D
UNS Electric	E-04204A-06-0783	35.59	E
Southwest Gas Corporation	G-01551A-07-0504	39.53	F
Notes and Source:			
[A]: APS workpaper JCL-WP11, p.9			
[B]: TEP Schedule B-5, p. 3			
[C]: UNSG Schedule B-5, p. 3			
[D]: UNSE Schedule B-5, p. 3			
[E]: UNSE filing Schedule B-5, p. 3			
[F]: SWG Schedule B-5, p. 2			

The revenue lags used by AAWC of over 45 days are considerably longer than the comparable revenue lags used in each of these recent rate cases by other large Arizona utilities that bill their customers monthly.

**Q. Please summarize your recommendation for adjusting AAWC's revenue lag and describe how the adjusted revenue lags you are recommending for AAWC compare**

•  
1 with the revenue lags used in recent rate cases by other large Arizona utilities that  
2 bill their customers monthly.

3 A. The adjusted revenue lags I am recommended for AAWC are shown Attachments RCS-6  
4 and RCS-7, Schedule B-4, for each district.<sup>9</sup> The adjusted revenue lags I am  
5 recommending are near or slightly above the high end of the range of revenue lags used  
6 by other large Arizona utilities that bill their customers monthly. This supports the  
7 reasonableness of, and need to use, the revised revenue lags. Also, because the revised  
8 revenue lag days recommended for AAWC are at, or slightly above, the high end of the  
9 range that has been used by other Arizona utilities, this supports viewing their use as the  
10 maximum revenue lag days that would be reasonable to use in determining AAWC's  
11 revenue requirement in this case.  
12

13 2. Service Company Payment Lag

14 Q. What lag did AAWC apply in its lead-lag study for payments of affiliated company  
15 Management Fees?

16 A. AAWC applied a payment lag of 14.7715 days, as shown on line 7 of AAWC's Schedule  
17 B-6, in the "Expense Lag Days" column for each district. However, AAWC indicated in  
18 response to a RUCO data request that it wanted to drastically revise this lag and instead  
19 reflect a pre-payment of the affiliated Management Fees. Specifically, in response to  
20 RUCO 2-75, AAWC has indicated that it pre-pays the affiliated Service Company for  
21 such affiliated Management Fees and wants to revise its filed lead-lag study to reflect a  
22 pre-payment, on average, of 11.25 days. In its rebuttal filing, AAWC has now sought to  
23 include a prepayment of affiliated Service Company charges in its CWC calculation.

---

<sup>9</sup> The adjusted Revenue Lag for each AAWC district being recommended has not changed since my direct testimony.

1  
2 **Q. Does AAWC's rebuttal convince you that a pre-payment of Management Fees to the**  
3 **affiliates be allowed in the lead-lag study?**

4 **A.** No. AAWC witness Gutowski addresses this at pages 9-11 of her rebuttal testimony. She  
5 claims that the prepayment of affiliate Management Fees should be allowed because:

- 6 • "the majority of the Service Company bill is paid in Advance"<sup>10</sup>
- 7 • All of the American Water Works operating companies signed a Service Company  
8 agreement in 1989.<sup>11</sup>
- 9 • That Service Company Agreement contains an Article IV, Billing Procedures,  
10 which AAWC apparently believes should dictate the payment lag results for  
11 ratemaking purposes.<sup>12</sup>
- 12 • Not allowing the Service Company prepayment proposed by AAWC in the current  
13 rate case would "increase the Service Company's cost of working capital."<sup>13</sup>
- 14 • The alleged additional Service Company costs "would then be passed back through  
15 the Service Company bill to Arizona in the form of higher Service Company  
16 costs."<sup>14</sup>
- 17 • The Service Company agreement terms are reasonable.<sup>15</sup>
- 18 • The pre-payment of Management Fees to the affiliated Service Company reflects  
19 actual lead days.<sup>16</sup>

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<sup>10</sup> See, Gutowski rebuttal, page 10, lines 9-10.

<sup>11</sup> Id, line 13.

<sup>12</sup> Id, lines 13-20.

<sup>13</sup> Id., lines 21-23.

<sup>14</sup> Id, lines 23-25

<sup>15</sup> See, Gutowski rebuttal, page 11, lines 1-2.

<sup>16</sup> Id., lines 4-5.

- “This is the same kind of lead days used in the 2008 Working Capital calculation that was approved as part of Decision 71410.”<sup>17</sup>

**Q. Has AAWC demonstrated that the Service Company agreement it is relying upon was ever approved by the Arizona Corporation Commission for any of the districts at issue in the current AAWC rate case?**

**A.** No. RUCO 2-76 asked the Company, in part: “Has the Commission approved any agreement between AzAWC and the affiliated Service Company? If not, explain fully why not. If so, please identify and provide a complete copy of such agreement. Include all amendments and changes thereto since AzAWC’s last rate case.”

AAWC’s response stated, among other things, that<sup>18</sup>:

Prior approval of an affiliate arrangement is not required in Arizona. **The Company has searched the Commission’s decisions listing and has not been able to locate a case decision in which either the Company requested approval of or such approval was granted of the agreement between Arizona American and the Service Company (“Agreement”). We believe neither has occurred**, but we are not 100% certain at this time whether or not the ACC has approved the Agreement because the Company was providing utility services in Arizona for many years but only in the Paradise Valley district and readily available decisions for the 1990s are not complete.  
(Emphasis supplied.)

AAWC included with its response to RUCO 2-76 a copy of the Paradise Valley “Agreement.” Paradise Valley is not among the districts for which revenue increases are being sought in the current AAWC rate case. Consequently, AAWC has not been able to demonstrate that the Arizona Corporation Commission has approved the Service

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<sup>17</sup> Id, lines 5-7.

<sup>18</sup> A complete copy of AAWC’s response to RUCO 2-76 is included in Attachment RCS-4.

1 Company Agreement as it applies to any of the AAWC districts covered in the current  
2 AAWC rate case. AAWC should not be allowed to bootstrap a 20-year old affiliate  
3 agreement for Paradise Valley onto the more recently acquired districts whose rates are at  
4 issue in the current AAWC rate case, especially when such an agreement contains terms  
5 that are unreasonable, such as the term pertaining to prepayment of affiliate Management  
6 Fees.

7  
8 **Q. If the Service Company agreement AAWC is relying upon was never approved by**  
9 **the Arizona Corporation Commission for any of the districts at issue in the current**  
10 **AAWC rate case, should it dictate the result for ratemaking purposes as it pertains**  
11 **to the lead-lag study?**

12 A. No. Not only was the Service Company agreement relied upon by AAWC apparently  
13 never approved by the Commission for any of the districts included in the current AAWC  
14 rate case, requiring prepayment of affiliated Management Fee charges would be *prima*  
15 *facie* unreasonable, and such a provision should be rejected in any event for ratemaking  
16 purposes.

17  
18 **Q. Why is prepayment of affiliate Management Fees unreasonable?**

19 A. This is not an arm's length transaction. It is an affiliated transaction. In order to protect  
20 ratepayers from abuses, utility affiliated transactions must be carefully scrutinized. The  
21 prepayment provision in the affiliated Service Company agreement does not pass the  
22 reasonableness test for ratemaking purposes and should therefore be rejected. If AAWC  
23 were obtaining the services from a third party, normal commercially reasonable payment

1 terms would apply. As evidenced by AAWC's payment lags to non-affiliated vendors and  
2 to AAWC's own employees, such terms would not prepay for services before such  
3 services were provided.

4 As an example, AAWC does not pre-pay the salaries and wages for its own work  
5 force. AAWC ratepayers should not be required to pay for extra amounts of return on rate  
6 base for Cash Working Capital that has been produced by an affiliated arrangement that  
7 involves pre-paying for affiliated Service Company payroll just because the employees  
8 providing the service are located in an affiliate for purposes of the overall corporate  
9 organizational structure.

10  
11 **Q. Please respond to Ms. Gutowski's claim that "This is the same kind of lead days used**  
12 **in the 2008 Working Capital calculation that was approved as part of Decision**  
13 **71410."**

14 **A.** If an issue were not identified and contested in a particular rate case, or was overlooked in  
15 a case, apparently AAWC witness Gutowski believes that it should not or cannot therefore  
16 ever be challenged or adjusted in a subsequent rate case, when it is identified and  
17 contested. It does not appear that an issue relating to the prepayment of affiliated  
18 Management Fees was discussed in Decision No. 71410. Moreover, AAWC's own direct  
19 filing in the current AAWC rate case did not reflect a prepayment of affiliated Service  
20 Company charges in AAWC's lead-lag study. It appears that AAWC's reliance upon  
21 Decision No. 71410 for an issue that was not specifically discussed in that decision may  
22 be misplaced.

1 **Q. Please respond to Ms. Gutowski's claims that "[n]ot allowing the Service Company**  
2 **prepayment proposed by AAWC in the current rate case would "increase the Service**  
3 **Company's cost of working capital" and that the alleged additional Service Company**  
4 **costs "would then be passed back through the Service Company bill to Arizona in the**  
5 **form of higher Service Company costs."**

6 **A.** Ms. Gutowski has provided no support for such claims. AAWC has claimed that the  
7 affiliated Service Company was providing services "at cost."<sup>19</sup> In the current AAWC rate  
8 case I have reviewed a number of responses concerning affiliated Management Fee  
9 charges to AAWC, and have not seen a Service Company working capital or return  
10 component clearly set forth in such documentation. If there is some type of working  
11 capital-based return, or other form of shareholder profit, embedded in the affiliated  
12 Management Fee charges to AAWC, this may point to a need for a thorough audit of such  
13 affiliated charges and may necessitate a more detailed examination of the underlying basis  
14 for such charges, especially if such charges include an affiliated company return  
15 component that has not been clearly disclosed and documented by the Company.

16 Finally, it is doubtful at best that a ratemaking adjustment for AAWC's cash  
17 working capital in the current case would have a direct impact on the Service Company's  
18 cost, or that this ratemaking adjustment would cause the affiliated charges from the  
19 Service Company to AAWC for Management Fees or other items to be higher in the  
20 future.

21  

---

<sup>19</sup> See, e.g., Gutowski rebuttal testimony at page 10, line 21.



1    **Q.    Should a pre-payment of Management Fees to the affiliates be allowed in the lead-lag**  
2           **study?**

3    A.    No, it should not.

4  
5    **Q.    Please explain your recommended Service Company payment lag.**

6    A.    The payment lag applied to Management Fees paid to the affiliate American Water Works  
7           Service Company ("AWWSC") and/or to other affiliates should be adjusted to  
8           commercially reasonable terms. This substantial affiliated transaction should not be  
9           permitted to unnecessarily increase rate base via the creation of an unreasonable CWC  
10          requirement. In its filed lead-lag study, AAWC reflected a payment lag of 14.7715 days  
11          that appears to be commercially reasonable, in that it is between the payroll lag of 12 days  
12          and the maintenance lag of 33.6 days, and thus is within a range of reasonableness.  
13          However, as stated in response to RUCO 2-75, and in AAWC's rebuttal, AAWC now  
14          seeks a revision to its filed lead-lag study to reflect a pre-payment, on average, for the  
15          Management Fees from the affiliates. This would imply that AAWC pays for affiliated  
16          services, on average, before the affiliated services are provided. AAWC should not be  
17          required to pay for services provided by this affiliate any more rapidly that it would pay  
18          for the services if they had been performed internally. Moreover, if AAWC chooses to  
19          pre-pay for affiliate-provided services, on average, before they are provided, ratepayers  
20          should not be required to pay a return on the increase to AAWC's rate base that relates to  
21          such pre-payment for affiliated services. I have adjusted the CWC associated with  
22          AAWC's payments to the affiliate AWWSC by applying the same 12-day expense lag  
23          associated with AAWC's direct labor costs.

1

2 **Q. What has AAWC said about this adjustment in its rebuttal?**

3 A. As noted above, AAWC witness Gutowski has claimed, among other things, that a 1989  
4 Service Company Agreement between AWWSC and the operating utility company would  
5 require prepayment by the utility of each month's Service Company costs.

6

7 **Q. Was AAWC able to demonstrate that the Arizona Corporation Commission had ever**  
8 **approved the Service Company Agreement as it applies to any of the AAWC districts**  
9 **covered in the current AAWC rate case?**

10 A. No. As noted above, AAWC has not been able to demonstrate that the Arizona  
11 Corporation Commission had ever approved the Service Company Agreement as it applies  
12 to any of the AAWC districts covered in the current AAWC rate case.

13

14 **Q. Even if the Arizona Corporation Commission had approved such a Service Company**  
15 **"Agreement", does that necessitate that a prepayment of affiliate Management Fees**  
16 **should be reflected in the utility's lead-lag study for ratemaking purposes?**

17 A. Apparently, not. The review of what is reasonable for ratemaking purposes typically  
18 occurs when an issue arises in the context of a rate case. As noted in my direct testimony,  
19 the West Virginia Public Service Commission ("PSC") addressed a similar issue in a  
20 recent rate case for one of AAWC's affiliated water companies operating in that  
21 jurisdiction. In West Virginia PSC Case No. 08-0900-W-42T, West Virginia American  
22 Water Company ("WVAWC") presented a similar argument, citing the provisions of its  
23 Service Agreement with AWWSC, and claiming that such Agreement would somehow

1 require WVAWC ratepayers to pay a return on the rate base/CWC impact of such an  
2 affiliated services prepayment arrangement.

3  
4 **Q. How did the West Virginia PSC decide that issue?**

5 A. In its Commission Order dated March 25, 2009, the West Virginia PSC rejected the  
6 arguments presented by the water utility and adopted the adjustment recommended by the  
7 Consumer Advocate Division ("CAD"). Pages 35-36 of the West Virginia PSC's Order  
8 state as follows:

9 The Commission is not persuaded that the CAD recommendation is  
10 unreasonable or requires actions on the part of the Company that violate its  
11 agreement with AWWSC. The agreement allows AWWSC to provide a  
12 current bill 'as soon as practicable' after the last day of each month. It also  
13 provides that AWWSC provide an estimate of the bill for the next month.  
14 However, there is no provision for advance payment of the next monthly  
15 bill. While WVAWC should not act unreasonably in making payments to  
16 AWWSC, a lag comparable with its own payroll lags does not appear to be  
17 unreasonable, while an advance payment does appear to be unreasonable.  
18 The Commission will adopt this CAD adjustment to the Cash Working  
19 Capital.

20  
21 (Emphasis supplied)

22  
23 Consequently, the West Virginia Commission used the 12-day utility labor cost payment  
24 lag for the affiliated Service Company Management Fees in the lead-lag study.

25  
26 **Q. Please summarize your recommended adjustment to AAWC's lead-lag study for the**  
27 **lag for payments to the affiliate AWWSC for Management Fees?**

28 A. The revised lead-lag study presented in AAWC's rebuttal shows the same 12-day lag for  
29 that utility's direct payroll as did WVAWC's lead-lag study. I have applied this same 12-  
30 day lag for the AAWC direct payroll as a reasonable payment lag for payments to the

1 affiliate AWWSC, which provides services to WVAWC as well as AAWC. The use of  
2 AAWC's direct payroll lag as a lag for the affiliated Management Fees charged to AAWC  
3 is reasonable and appropriate whereas a prepayment would be unreasonable, as described  
4 above. A longer payment lag for the affiliated Service Company could potentially be  
5 justified, based on other payments to non-affiliated vendors and service providers.

6  
7 **Q. Please explain why a payment lag longer than 12 days could be reasonable for**  
8 **payments to this affiliate?**

9 A. As shown on AAWC – Anthem Water Schedule B-6, lines 14 and 15, for example,  
10 AAWC's overall weighted lags for Maintenance Expense and Other Operating Expenses  
11 are 33.6 and 30.0 days, respectively. Consequently, applying the 12-day lag for AAWC's  
12 direct payroll<sup>20</sup> as a payment lag for payments to the affiliate AWWSC is probably a bit  
13 conservative.

14  
15 **3. Other Expense Adjustments**

16 **Q. Have you also adjusted Cash Working Capital for each district for your**  
17 **recommended adjustments to operating expenses?**

18 A. Yes. Schedule B-4 for each district on Attachment RCS-6 (for water) and RCS-7 (for  
19 wastewater) also reflects adjustments for operating expense amounts.

20  

---

<sup>20</sup> See, RUCO Attachment RCS-6 and RCS-7, Schedule B-4, line 1, Labor, for each respective district which has a composite weighted payment lag of 12.00 days, meaning that payment is made, on average, 12 days after service is provided.

1 **4. Remove Chemical Expense**

2 **Q. Please explain the adjustment to remove Chemical Expense from the Cash Working**  
3 **Capital calculation.**

4 **A.** Staff removed Chemical Expense from the calculation of Cash Working Capital because  
5 Chemical Inventory is included in the 13-month average of Materials and Supplies.  
6 AAWC witness Gutowski agreed with this Staff adjustment. I also agree with the Staff's  
7 adjustment and have reflected the removal of Chemical Expense on Schedule B-4 of  
8 Attachments RCS-6 and RCS-7.

9  
10 **5. Remove Uncollectibles**

11 **Q. Please explain the adjustment to remove Bad Debt Expense from the Cash Working**  
12 **Capital calculation.**

13 **A.** Staff removed Bad Debt Expense from the calculation of Cash Working Capital because it  
14 does not involve a cash outlay, and therefore should have no corresponding expense lag  
15 days. AAWC witness Gutowski agreed with this Staff adjustment. I also agree with the  
16 Staff's adjustment and have reflected the removal of Bad Debt Expense on Schedule B-4  
17 of Attachments RCS-6 and RCS-7 by reflecting 20.31 day lags for Customer Accounting  
18 Expense.

19  
20 **Summary of Cash Working Capital Adjustments**

21 **Q. What is your adjusted Cash Working Capital allowance for each district?**

A. My recommended adjusted Cash Working Capital allowance is shown on Attachments RCS-6 and RCS-7, Schedule B-4 for each district. My recommended adjustment to AAWC's originally filed request, is summarized in the following table:

Summary of Adjustments to Cash Working Capital

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (122,000)	\$ (168,000)	\$ (130,000)	\$ (105,000)	\$ (113,000)	\$ (638,000)

**B-5 Youngtown Plant – Sun City Water**

**Q. Please explain your adjustment shown on Schedule B-5.**

A. This adjustment reflects the recommendation made by Staff witness Gerald Becker as it relates to reconciling items related to the Company's Youngtown Plant ("Youngtown") in the Sun City water district that Staff noted during its review of AAWC's workpapers in this proceeding. In response to Staff's inquiry, the Company stated that the amounts associated with Youngtown relate to a reconciling item between AAWC's books and the plant balances that were approved in the Company's last rate case. AAWC was unable to provide sufficient support for this item in this proceeding, thus Staff concluded that it should be removed from rate base. As shown on Attachment RCS-6, Schedule B-5, these adjustments reduce utility plant in service by \$149,497 and accumulated depreciation by \$22,008 for a net reduction to rate base in the amount of \$127,489 in the Sun City water district.

**Q. Has AAWC accepted Mr. Becker's adjustments to utility plant in service and accumulated depreciation as it relates to the Youngtown Plant?**

1 A. Yes. As stated on page 2 of her Rebuttal Testimony, Company witness Sandra L. Murrey  
2 stated that this plant item had been included in the Company's workpapers in this  
3 proceeding as a Staff reconciling item from AAWC's last rate case. The Company agreed  
4 with Mr. Becker's adjustments on the basis that AAWC may further research and support  
5 this item in a future rate case.  
6

7 **B-6 Verrado Wastewater Plant – Anthem/Agua Fria Wastewater**

8 **Q. Please explain your adjustment shown on Schedule B-6.**

9 A. This adjustment reflects the recommendation made by Staff witness Gary McMurry as it  
10 relates to the Company's Verrado Wastewater Plant ("Verrado"). Mr. McMurry stated  
11 that the Company's proposal to include the actual recorded cost of Verrado in rate base  
12 does not take into account that Verrado is overbuilt and under-utilized. Therefore, Staff  
13 concluded that the excess capacity associated with Verrado should be excluded from rate  
14 base and thus, removed \$1,838,637 from utility plant in service. As shown on Attachment  
15 RCS-7, Schedule B-6, I have reduced rate base by \$1,838,637 for Anthem/Agua Fria  
16 Wastewater.  
17

18 **Q. Has AAWC accepted Staff's recommended adjustment to reduce utility plant in**  
19 **service as it relates to Verrado?**

20 A. Yes. As stated on page 2 of her Rebuttal Testimony, Company witness Murrey stated that  
21 although AAWC has accepted Staff's recommendation to remove the excess capacity  
22 associated with Verrado from rate base, the Company requested that the Commission

1 determine that removing this excess capacity is temporary until a future rate case and that  
2 it is appropriate to include the \$1,838,637 in Plant Held For Future Use.

3  
4 **Q. Is Plant Held for Future Use included in rate base?**

5 A. No. It is not used and useful during the test year, and therefore Plant Held for Future Use  
6 is not included in rate base.

7  
8 **B-7 Comprehensive Planning Study – Sun City and Sun City West Wastewater**

9 **Q. Please explain your adjustment shown on Schedule B-7.**

10 A. This adjustment reflects the recommendation made by Staff to transfer costs totaling  
11 \$12,242 associated with a comprehensive planning study that was recorded in the Sun  
12 City Wastewater district to the Sun City West Wastewater district because this planning  
13 study was in fact conducted for Sun City West Wastewater. Therefore, as shown on  
14 Attachment RCS-7, Schedule B-7, I have reduced Sun City Wastewater's utility plant in  
15 service by \$12,242 and have increased Sun City West Wastewater's utility plant in service  
16 by the same amount. This resulted in changes to the rate base of these two districts. For  
17 the combined wastewater districts, this resulted in a net rate base adjustment of zero.

18  
19 **Q. Has AAWC accepted Staff's recommended adjustment to transfer the**  
20 **comprehensive planning study costs from Sun City Wastewater to Sun City West**  
21 **Wastewater?**



1 A. Yes. As stated on page 3 of her Rebuttal Testimony, Company witness Murrey concurred  
2 that the comprehensive planning study was conducted for Sun City West Wastewater and  
3 therefore, such costs should be transferred to that district.  
4

5 **B-8 North West Valley Treatment Plant – Anthem/Agua Fria and Sun City West**  
6 **Wastewater**

7 **Q. Please explain your adjustment shown on Schedule B-8.**

8 A. This adjustment reflects the recommendation made by Staff witness McMurry to update  
9 the allocation percentages associated with the North West Valley Treatment Plant  
10 (“NWVTP”) as it relates to the relative capacity demand between Anthem/Agua Fria  
11 Wastewater and Sun City West Wastewater. Staff recommended updating the NWVTP  
12 allocation to Anthem/Agua Fria Wastewater from 32 percent to 28 percent. In addition,  
13 Staff recommended updating the NWVTP allocation to Sun City West Wastewater from  
14 68 percent to 72 percent. As shown on Attachment RCS-7, Schedule B-8, updating the  
15 NWVTP allocation percentages results in a decrease to utility plant in service for  
16 Anthem/Agua Fria Wastewater in the amount of \$1,039,823 and an increase to utility  
17 plant in service for Sun City West Wastewater for the same amount. This results in  
18 changes to the rate base of these districts. For the combined wastewater districts, this  
19 results in a net adjustment to utility plant in service of zero.  
20

21 **Q. Is there a corresponding adjustment to accumulated depreciation related to the**  
22 **NWVTP allocation percentages?**

1 A. Yes. As shown on Attachment RCS-7, Schedule B-8, I have also incorporated Staff's  
2 recommendation to decrease accumulated depreciation for Anthem/Agua Fria Wastewater  
3 in the amount of \$630,244 and to increase accumulated depreciation for Sun City West  
4 Wastewater by the same amount, which results in a net adjustment to accumulated  
5 depreciation of zero.

6  
7 **Q. Has AAWC accepted Staff's recommended adjustment to update the allocation**  
8 **percentages associated with the NWVTP?**

9 A. Yes. As discussed in the Rebuttal Testimony of Company witness Linda J. Gutowski, the  
10 Company has accepted Staff's recommendation to update the allocation percentages  
11 associated with the NWVTP as it relates to the relative capacity demand between  
12 Anthem/Agua Fria Wastewater and Sun City West Wastewater.

13  
14 **Q. Do you have any other comments about this adjustment?**

15 A. Yes. Allocating the NWVTP more appropriately between these two districts, as  
16 recommended by Staff and accepted by AAWC, will also help to mitigate the rate  
17 increases for the Anthem/Agua Fria Wastewater district, which are among the highest of  
18 the districts in the current AAWC rate case.

19

20 **B-9 Accumulated Deferred Income Taxes**

21 **Q. Please explain your adjustment shown on Schedule B-9.**

22 A. This adjustment incorporates the recommendation made by Staff witnesses Becker and  
23 McMurry to reflect in rate base the accumulated deferred income taxes ("ADIT") that

1 were recorded in the Company's audited financial statements. AAWC proposed  
2 allocating ADIT of approximately \$13.026 million to each district in this proceeding  
3 based on its four-factor allocation, but Staff was unable to reconcile the \$13.026 million  
4 figure to the Company's audited financial statements' ADIT balance of \$12.689 million.  
5 As shown on Attachment RCS-6, Schedule B-9, and summarized in the table below, the  
6 incorporation of Staff's recommended adjustments reduces ADIT (thus increasing rate  
7 base) by a total amount of \$173,965.

	Anthem	Sun City	Anthem/ Agua Fria	Sun City	Sun City West	
District	Water	Water	Wastewater	Wastewater	Wastewater	Total
Adjusted TY Rate Base	\$ (18,580)	\$ (49,151)	\$ (27,084)	\$ (47,073)	\$ (32,077)	\$ (173,965)

8  
9  
10 As discussed on page 7 of the Rebuttal Testimony of Company witness Linda J.  
11 Gutowski, AAWC has agreed with Staff's recommendation to use the ADIT balance  
12 reflected in the Company's audited financial statements as the basis for allocating such  
13 ADIT to each of the districts in this proceeding.

14  
15 **Q. Does your reflection of the Staff-adjusted ADIT balance in the current AAWC rate**  
16 **case imply acceptance or endorsement of each component included in that ADIT**  
17 **balance?**

18 **A.** No. I have reflected the ADIT amounts on Schedule B-9 in part to help minimize issues;  
19 however, this should not be construed as an endorsement of each component included in  
20 the ADIT balance. AAWC's ADIT balance is a net addition to rate base and may include

1 components that would require adjustment in a future case if a detailed component-by-  
2 component analysis were undertaken.  
3

4 **Other Rate Base Adjustments**

5 **Q. Are there any additional adjustments that were recommended by Staff which were**  
6 **accepted by the Company?**

7 A. Yes, there are two additional adjustments that were recommended by Staff that were  
8 accepted by the Company. The first such adjustment relates to the transfer of \$22,289,  
9 which was for chemical feed and water quality monitoring equipment, that Staff  
10 recommended be reclassified from Account 304300 to Account 320100, for Anthem  
11 Water. The second such adjustment relates to the transfer of \$487,000, which was for a  
12 power generator, that Staff recommended be reclassified from Account 354400 to  
13 Account 355500, for Anthem/Agua Fria Wastewater.  
14

15 **Q. Are you presenting rate base adjustment schedules for these two adjustments?**

16 A. No. I have no reason to disagree with the appropriateness of these Staff-recommended  
17 adjustments which AAWC has accepted. Since both of these adjustments merely  
18 reclassify amounts from one plant account to another, there is no net impact on RUCO's  
19 proposed rate base. Therefore, it was not necessary to present rate base adjustment  
20 schedules for either of these adjustments.  
21

22 **Q. Did these adjustments affect Depreciation Expense?**

1 A. Yes. The adjustment between plant accounts affected Depreciation Expense. I show the  
2 impact on Schedules C-18 and C-19.  
3  
4

5 **IV. ADJUSTMENTS TO OPERATING INCOME**

6 **Q. Please describe how you have summarized RUCO's proposed adjustments to**  
7 **operating income.**

8 A. Attachments RCS-6 and RCS-7 includes for each water and wastewater district,  
9 respectively and in summary for the water systems and, separately, for the wastewater  
10 districts included in AAWC's filing, a Schedule C that shows AAWC's requested net  
11 operating income, RUCO adjustments, and RUCO's adjusted net operating income.  
12 AAWC's proposed adjusted test year net operating income from its direct filing and  
13 RUCO's recommended adjusted net operating income for each district is summarized in  
14 the following table:

**Net Operating Income Summary - Water and Wastewater Districts**

District	Per Company		
	As-Filed	Per RUCO	Difference
Anthem Water	\$ 514,448	\$ 683,807	\$ 169,359
Sun City Water	\$ 861,085	\$ 1,359,588	\$ 498,503
Subtotal - Water	\$ 1,375,533	\$ 2,043,394	\$ 667,861
Anthem/Agua Fria Wastewater	\$ (191,785)	\$ (4,298)	\$ 187,487
Sun City Wastewater	\$ (51,593)	\$ 68,704	\$ 120,297
Sun City West Wastewater	\$ 618,443	\$ 748,629	\$ 130,186
Subtotal - Wastewater	\$ 375,065	\$ 813,034	\$ 437,969
Total	\$ 1,750,598	\$ 2,856,428	\$ 1,105,830

1 Attachments RCS-6 and RCS-7 also contain a Schedule C.1 for water, for wastewater, and  
2 for each district that presents RUCO's recommended adjustments to Arizona test year  
3 revenues and expenses. The impact on state and federal income taxes associated with  
4 each of the recommended adjustments to operating income is also reflected on Schedule  
5 C.1. The recommended adjustments to operating income are discussed below in the same  
6 order as they appear on Schedule C.1 of Attachments RCS-6 and RCS-7 for water and  
7 wastewater district, respectively.  
8

9 **C-1 Customer Annualization Correction (Anthem Water District)**

10 **Q. Please explain RUCO Adjustment C-1.**

11 A. AAWC's response to RUCO 2-48 says that RUCO witness Rodney Moore<sup>21</sup> found errors  
12 in the Company pro forma annualization for Anthem Water, which the Company is  
13 accepting and would reflect in their rebuttal. RUCO Adjustment C-1 in Attachment RCS-  
14 6 reflects the correction of such errors in computing the revenue requirement for Anthem  
15 Water. In my direct testimony, I had mistakenly decreased the amount of annualized  
16 revenue at current rates for Anthem Water by \$9,456. AAWC witness Gutowski has  
17 accepted this adjustment and pointed out that it should increase revenue, not decrease it,  
18 by \$9,458. I have revised Schedule C-1 in Attachment RCS-6 to reflect this correction.  
19

20 **C-2 Rate Case Expense (All Districts)**

21 **Q. What has AAWC requested for rate case expense?**

---

<sup>21</sup> Mr. Moore is presenting the rate design testimony for RUCO.

1 A. AAWC had requested \$678,425 for the current case, amortized over three years, plus  
2 amortization of the remaining unamortized balance from prior rate cases. The \$678,425  
3 proposed by AAWC for the current rate case is shown on AAWC witness Broderick's  
4 Exhibit TMB-2. The amounts requested for the prior rate cases of \$149,119 is from  
5 AAWC witness Kiger's direct testimony at page 10 and was requested over three years as  
6 an amortization in AAWC adjustment MHK-8. AAWC witness Kiger has agreed on page  
7 17 of his rebuttal testimony to remove the expense related to the prior rate case. AAWC  
8 witness Broderick's rebuttal at pages 5-6, however, continues to request an amount of  
9 \$678,425 for the current rate case. As noted in my direct testimony, this request is higher  
10 than the amount from the prior AAWC rate case.

11  
12 **Q. Why does the Company state it is asking for more rate case expense than in Docket**  
13 **No. 08-0227?**

14 A. Page 11 of AAWC witness Broderick's direct testimony stated that:

15 The primary reason this [\$678,425] estimate is higher than the most recent (seven  
16 district) rate case is primarily due to the anticipated additional requirement to  
17 provide a required public notice to all 154,000 Arizona-American customers of the  
18 proposed consolidated rates – at a cost of roughly \$95,957. There is additional  
19 cost to have our rate design expert, Mr. Paul Herbert, design, support and explain  
20 consolidated rates. We also anticipate mailing a postcard to all customers  
21 concerning public meetings about rate consolidation at a cost of approximately  
22 \$40,000.

23  
24 AAWC Exhibit TMB-2 presents an itemization of the Company's estimated rate case  
25 expense, by component, which sums to the \$678,425.

26 In addition to the components mentioned above, this includes \$230,000 for legal  
27 representation, \$65,000 for a cost of equity witness, \$65,000 for a rate design witness,  
28 \$15,000 for compliance for an Anthem rate tiers study, \$75,000 for "Shared Services"

1 which appears to be for affiliate labor-related charges, \$20,000 for newspaper publishing  
2 of initial public notice and ACC public comment meetings, \$47,500 related to Company-  
3 sponsored community meetings, and \$50,329 for an initial public notice letter to 81,176  
4 customers.

5 Mr. Broderick's rebuttal testimony at page 6 states that, as of March 11, 2010, the  
6 Company had incurred \$226,339 in rate case expense for the current case. Additionally,  
7 he states that in a procedural order dated March 18, 2010, the ALJ required a Company-  
8 wide all customer notice regarding rate consolidation, which AAWC anticipates will be  
9 sent as a first class letter at a total cost of approximately \$55,000. He also states that the  
10 majority of external legal costs are still ahead.

11  
12 **Q. Have some components of the Company's initial estimate of cost for the current rate**  
13 **case not materialized as expected?**

14 **A.** Yes. A request for the Company's supporting documentation for its rate case expense was  
15 made in RUCO 2-40(a). With regard to the initial public notice, the response to RUCO 2-  
16 40(a) stated: "Overall, to-date, expenses are running slightly under budget because the  
17 initial required public notice was sent as a bill insert and not as a separately mailed  
18 letter. However, legal expenses are expected to later be over budget." (Emphasis  
19 supplied.) Company Exhibit TMB-2 listed an estimated expense of \$50,329 for the initial  
20 public notice.  
21



1     **Q.     Has AAWC explained why, if the initial notice was sent as a bill insert and saved**  
2           **approximately \$50,000, the notice concerning rate consolidation could not also be**  
3           **sent as a bill insert?**

4     **A.     No.** Although he discusses the notice on page 6 of his rebuttal testimony, Mr. Broderick  
5           does not clearly indicate why the notice concerning rate consolidation could not also be  
6           sent as a bill insert, thus similarly saving on postage, similar to the initial notice.

7  
8     **Q.     Has the Company's identified how much of the \$226,339 in rate case expense it states**  
9           **it has incurred through March 18, 2010 is for Company and affiliate labor?**

10    **A.     No.**

11  
12    **Q.     What regulatory concerns are raised by charging for Company or affiliate labor cost**  
13           **in rate case expense?**

14    **A.     Concerns of double-counting are raised by charging for Company or affiliate labor cost in**  
15           rate case expense. Payroll costs and costs for affiliate labor are included elsewhere in the  
16           Company's filing, based on adjusted test year amounts. Affiliated company labor and  
17           expenses incurred subsequent to the test year as rate case cost would represent an increase  
18           to the amount recorded during the test year. Costs for Company and affiliate labor should  
19           therefore be excluded from rate case expense to preclude double counting or excessive  
20           charges to ratepayers.

21  
22    **Q.     How does the amount for rate case cost requested by AAWC for the current case**  
23           **compare with rate case expense allowed in prior AAWC rate cases?**

1 A. Even though there are fewer districts in the current AAWC rate case, the rate case expense  
2 claimed by AAWC is considerably higher than the amount that was allowed in Decision  
3 No. 71410 from AAWC's last rate case. Decision No. 71410 states at page 39 that: "We  
4 find total rate case expense of \$456,275, normalized over three years and allocated across  
5 the seven districts using the Company's 4-factor allocation methodology as agreed to by  
6 Staff to be reasonable, and will allow it." (footnote omitted).

7  
8 **Q. Has the Company identified the allowed amounts of rate case expense in other recent**  
9 **AAWC rate cases?**

10 A. Yes. The Company's response to RUCO 2-78(b) states that:

11 Decision No. 71410, dated December 8, 2009, allowed \$456,275 in a seven district  
12 rate case. Decision No. 70372, dated June 13, 2008 allowed \$300,000 in a three  
13 district rate case. Decision No. 70351, dated May 16, 2008 allowed \$94,264 in a  
14 one district rate case.

15  
16 AAWC's response to RUCO 2-78(c) states "The amortization period for Decisions 71410  
17 and 70372 was three years and Decision 70351 was four years."

18  
19 **Q. Should AAWC's allowed rate case expense be based on continued updates of actual**  
20 **costs, as Mr. Broderick recommends at page 5 of his rebuttal testimony?**

21 A. No. At page 5 of his rebuttal, Mr. Broderick suggests that AAWC be allowed to use  
22 actual rate case cost, which he offers to update "at hearing, in the Company's post hearing  
23 exhibits or even later in the Company's post hearing brief." Allowing constant updates at  
24 such late stages as a basis for the allowance could remove existing incentives to control  
25 such cost, and may not provide for adequate review or questioning of such costs by other  
26 parties, if such "updates" are provided after the record is closed. The ratemaking

allowance for rate case expense should be based on a reasonable normalized amount, not necessarily on how much a utility actually records for such expense through the end of a rate case. Additionally, as noted above, there are concerns with AAWC and affiliated labor charges being included in rate case expense. Consequently, I do not believe there would be any benefit to allowing AAWC to update its rate case expense amount, especially for periods after the hearing, and therefore recommend that this proposal by Mr. Broderick be rejected.

**Q. Please explain RUCO Adjustment C-2.**

A. This adjustment removes the cost for the prior rate case, and provides for an allowance of \$460,000 for the current case, normalized over three years, for a normalized annual allowance of \$153,333. This normalized allowance is allocated to each district in proportion to its four-factor allocator, as shown on Schedule C-2 in Attachment RCS-6 for water and Attachment RCS-7 for wastewater, respectively. The adjustment to reduce AAWC's requested rate case expense for each district is summarized below.

Summary of Adjustments to Rate Case Expense

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (27,003)	\$ (24,304)	\$ (31,679)	\$ (20,573)	\$ (18,954)	\$ (122,513)

**Q. Has RUCO Adjustment C-2 changed as a result of AAWC's rebuttal?**

A. No. A total allowance of \$460,000 normalized over three years, and the removal of AAWC's prior rate case expense is consistent with the recommendations made concerning rate case expense in my direct testimony. The \$460,000 total allowance is also larger than

1 the amount allowed from Decision No. 71410, dated December 8, 2009, in a seven district  
2 rate case.

3  
4 **C-3 Incentive Compensation Expense – AAWC Employees (All Districts)**

5 **Q. Please explain RUCO Adjustment C-3.**

6 A. This adjustment removes 30 percent of the incentive compensation expense for AAWC  
7 employees that the Company had included in the test year.

8  
9 **Q. How did you determine the amount of incentive compensation for AAWC employees**  
10 **that the Company had included in the test year, inclusive of pro forma adjustments?**

11 A. The amount was determined based on the Company's responses to RUCO data requests,  
12 which had asked for such information, and from a review of underlying detail contained in  
13 the Excel files that were provided by the Company. The 30 percent disallowance has also  
14 been applied by the Commission to AAWC's incentive compensation expense in other  
15 recent AAWC rate cases including Docket Nos. W/SW-01303A-08-0227, as discussed in  
16 Decision No. 71410.

17  
18 **Q. What has AAWC stated in rebuttal concerning incentive compensation for AAWC**  
19 **employees?**

20 A. AAWC witness Townsley states at pages 6-7 of his rebuttal testimony that a 30 percent  
21 reduction for AAWC employees' incentive compensation is appropriate. He disagrees  
22 with a 50 percent disallowance, which is the disallowance percentage that the Commission  
23 has applied for other Arizona utilities' incentive compensation expense.

1           At page 7 of his rebuttal testimony Mr. Townsley claims that no justification or  
2 even explanation was provided in my direct testimony as to why the Commission should  
3 remove the Annual Incentive Plan ("AIP") incentive compensation included in the affiliate  
4 Management Fee charges from AAWC's expense.

5           At pages 7-8, he quotes from Commission Decision No. 71410 where 30 percent  
6 of AAWC's incentive compensation expense was disallowed.

7           At pages 8-9, he also quotes from a West Virginia Public Service Commission  
8 decision where that commission had rejected an adjustment to remove the cost of  
9 incentive compensation.

10          At page 7, lines 7-9, he also claims that: "This type of incentive compensation  
11 would need to be discontinued if the Commission were to deny additional amounts, which  
12 would ultimately result in a greater offsetting increase for employee base pay with no  
13 performance contingency."

14  
15 **Q. Did the Company provide a copy of its incentive compensation plan?**

16 A. Yes, a copy was provided in response to RUCO 2-6.  
17

18 **Q. Please briefly discuss the key provisions of the incentive compensation program.**

19 A. According to the 2008 Annual Incentive Plan - Rewarding Achievement, the annual  
20 incentive plan ("AIP" or "Plan") is designed to reward participants for the performance  
21 results attained by such participants and the Company during the plan year. These  
22 performance standards are comprised of the three following components: (1) Financial  
23 (Corporate, Divisional/Regional and State), Operational and Individual.

*Financial Component*

The financial component is based on operating income. The performance level is determined at the Corporate, Divisional/Regional and State levels. **In 2008, more than 85% of the operating income target for the entire Company had to be achieved before incentive compensation was awarded based on the corporate financial component of the Plan**, although such an award could be made on the Divisional/Regional and State financial components if operating income exceeded 85% of the target. In addition, **more than 75% of the Corporate operating income target had to be achieved in order for any payments to be made on any components of the Plan for the entire Company.**

*Operational Component*

The operational component is based on the following:

- Environmental Compliance: Environmental compliance is measured by "Notice of Violation ("NOV") count defined as the number of times an official notice is issued by a primacy agency for failure to comply with a federal, state or local government statute or regulation that is covered under the scope of the American Water Environmental Management Policy.
- Safety Performance: Safety performance is measured on an OSHA Total Recordable Incident Rate ("ORIR") which is defined as the rate of total injuries requiring treatment beyond first aid per 200,000 hours worked. ORIR focuses on total injury reduction which by extension improves Lost Work Day Case Rate ("LWCR") and correlates more closely to workers compensation claims and costs. LWCR will remain a personal performance goal for the Operations and Operational Risk Management functions.
- Customer Satisfaction: Customer satisfaction is based on the results of the annual Customer Satisfaction Survey ("CSS") conducted in the fourth quarter of each year through randomly selected customer contacts in each state.

- Service Quality: Service quality is based on the annual results of the Service Quality Surveys ("SQS") conducted throughout the year with customers having had recent contact with a customer service or field service representative.
- Service Level: Percentage of calls answered in the Customer Service Center within a certain timeframe.
- Quality Measures (Shared Services Center): (1) SSC error rate – number of financial statement errors; (2) Reconciliations – calendar year average of accounts beyond policy; and (3) Timeliness of Processes – annual percentage of processes conducted according to schedule (e.g. tax filings, consolidated financial statements, external audit information submissions, days to image & process invoices and Orcom rate changes.
- Compliance (Shared Services Center ("SSC")) – (1) External audit findings – number of unrecorded differences and topside entries; (2) internal audit findings – number of instances of deviations from policy/procedures during SOX testing; and (3) external filing requirements – annual reports and Commission reports completed by established deadlines for SSC.

Each operational component discussed above is measured as follows:

Environmental Compliance – 25%  
Safety Performance – 25%  
Customer Satisfaction – 25%  
Service Quality – 25%

#### *Individual Component*

The individual component includes Performance Targets as agreed to by participants and managers within the Companywide standard performance management process. The Company will provide an AIP letter which outlines the Company component targets. Individual performance is assessed using American Water's Performance Management and Development Review ("PDR") process whereby the PDR requires each individual to have five performance targets. Each of these five performance targets should be specific, measurable and aligned with the Company's performance targets.

1     **Q.   What criteria has the Commission found important in deciding issues concerning**  
2     **utility incentive compensation in recent cases?**

3     A.   The criteria the Commission has found important in deciding this issue in recent cases are  
4     described in various orders which have addressed the treatment of utility incentive  
5     compensation expense for ratemaking purposes. In Decision No. 68487 (February 23,  
6     2006), the Commission adopted Staff's recommendation for an equal sharing of costs  
7     associated with the Southwest Gas Corporation's ("SWG") Management Incentive Plan  
8     ("MIP") expense. For example, in reaching its conclusion regarding SWG's MIP, the  
9     Commission stated in part on page 18 of Order 68487 that:

10           We believe that Staff's recommendation for an equal sharing of the costs  
11           associated with MIP compensation provides an appropriate balance between  
12           the benefits attained by both shareholders and ratepayers. Although  
13           achievement of the performance goals in the MIP, and the benefits attendant  
14           thereto, cannot be precisely quantified there is little doubt that both  
15           shareholders and ratepayers derive some benefit from incentive goals.  
16           Therefore, the costs of the program should be borne by both groups and we  
17           find Staff's equal sharing recommendations to be a reasonable resolution.  
18

19           AAWC has not refuted the fact that both shareholders and ratepayers derive some benefit  
20           from incentive goals when such goals are achieved by AAWC employees.  
21

22     **Q.   Do AAWC's shareholders and customers both benefit from the achievement of**  
23     **incentive compensation program?**

24     A.   Yes. Shareholders benefit from the achievement of financial goals. Additionally,  
25     shareholders benefit from the achievement of expense reduction and expense containment  
26     goals between rate cases. Shareholders and ratepayers can both benefit from the  
27     achievement of customer service goals.



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**Q. Why have you used a 30 percent disallowance for the incentive compensation for AAWC employees?**

A. Although a higher disallowance percentage could perhaps be justified (the Commission has disallowed 50 percent of other Arizona utilities' incentive compensation expense based on an equal sharing of the cost between shareholders and ratepayers), I used a 30 percent disallowance for incentive compensation of AAWC employees because this is what the Commission had determined for AAWC incentive compensation in recent prior AAWC rate cases, including Decision Nos. 71410 and 68858. Decision No. 68858 at page 20-21, for example, stated that:

RUCO recommends that \$12,795 of the Company's proposed \$20,037 AIP, Performance Pay and Stay Bonuses be disallowed. RUCO recommends disallowing 30 percent, or \$5,555 of the \$18,517 in Arizona Corporate allocated management fees related to the Company's Annual Incentive Plan expenses, because 30 percent of the AIP is directly related to Company financial performance measures and 70 percent to operational and individual performance measures. ... RUCO argues that the 30 percent portion of AIP expenses based on financial performance measures benefit only shareholders. ...

We agree with RUCO that shareholders are the primary beneficiaries of additional profit the Company achieves as the result of the Company meeting its financial targets, and therefore find RUCO's proposal to disallow the 30 percent of AIP that is based on the Company's financial performance measures to be reasonable and appropriate. ... An adjustment reducing AIP expenses by \$5,555 is appropriate and should be adopted.

In Decision No. 68858, the Commission did not adjust expense for AAWC's Performance Pay and Stay Bonuses because they were deemed closely related to salary expense. The Commission did adjust the incentive compensation portion that was related to meeting financial targets.

1           Decision No. 71410 at page 35 indicates that RUCO proposed a disallowance of  
2           30 percent, or \$5,555, of the Company's \$18,517 Arizona Corporate allocated annual  
3           incentive pay ("AIP") management fee expenses for the districts in this proceeding. Staff  
4           agreed with the adjustment and the Company indicated, while it disagrees with the  
5           premise that shareholders are the primary beneficiaries of additional profit the Company  
6           achieves as a result of Arizona-American meeting its financial targets, it did not oppose  
7           RUCO's adjustment in that proceeding.

8           Consequently, the Commission used a 30 percent disallowance of the AAWC  
9           incentive compensation that resulted from Arizona-American meeting its financial targets.

10  
11   **Q.   Did you detect anything missing in the analysis of AAWC's incentive compensation**  
12   **in those prior cases?**

13   A.   Apparently, the parties to those prior cases did not attempt to distinguish the source of the  
14   financial trigger leading to the payment of incentive compensation. Arizona-American  
15   meeting its financial targets can be a vastly different situation from the corporate parent  
16   entity, American Water Works, meeting its financial targets. American Water Works'  
17   corporate financial income is only moderately influenced by AAWC profits and is heavily  
18   influenced by non-Arizona jurisdictional operations, and is also impacted by American  
19   Water Works' non-regulated operations. AAWC ratepayers should not have to pay for  
20   incentive compensation expense that is premised on American Water Works' non-Arizona  
21   jurisdictional operations or non-regulated operations-based financial achievements.

22

1   **Q.    Why have you used a 100 percent disallowance for the incentive compensation for**  
2       **affiliated Service Company employees who charge AAWC via the Management Fee?**

3   **A.    I have recommended disallowing 100 percent of the incentive compensation for the**  
4       **affiliated Service Company employees who charge AAWC via the Management Fee**  
5       **because the award to Service Company employees is dependent upon corporate operating**  
6       **income and corporate financial targets. This is influenced by operating income of non-**  
7       **jurisdictional and non-regulated operations of American Water Works. Arizona**  
8       **ratepayers should not have to pay for incentive compensation that is tied to American**  
9       **Water Works' corporate or non-jurisdictional and non-regulated income. The AIP plan**  
10      **indicates that, in 2008, more than 85% of the operating income target for the entire**  
11      **Company had to be achieved before incentive compensation was awarded based on the**  
12      **corporate financial component of the Plan, although such an award could be made on the**  
13      **Divisional/Regional and State financial components if operating income exceeded 85% of**  
14      **the target. In addition, more than 75% of the Corporate operating income target had to be**  
15      **achieved in order for any payments to be made on any components of the Plan for the**  
16      **entire Company. Consequently, I believe it is reasonable and appropriate to exclude 100**  
17      **percent of the incentive compensation expense that is charged to AAWC for affiliated**  
18      **Service Company employees as part of the American Water Works Management Fee**  
19      **charges.**

20  
21   **Q.    Have some of AAWC's affiliates in other jurisdictions removed 100 percent of**  
22       **incentive compensation expense in recent rate cases because payment is premised on**  
23       **a parent company financial trigger?**

1 A. Yes. As an example, in Docket No. 09-0319, before the Illinois Commerce Commission,  
2 Karla O. Teasley, the President of Illinois-American Water Company ("IAWC") testified  
3 concerning incentive compensation as follows:

4 VII. INCENTIVE COMPENSATION

5 Q28. Has the Company proposed recovery of expense related to payments under  
6 an incentive compensation plan?

7 A. No. In the Docket 07-0507 Order, the Commission denied recovery of  
8 incentive compensation expense due to the presence of a parent company  
9 financial trigger. In recognition of the Commission's concern as stated in Docket  
10 07-0507, IAWC will not propose recovery of this cost.  
11 (Emphasis supplied.)  
12

13 A copy of such testimony is included in Attachment RCS-8.

14 The same parent company financial trigger that caused denial of recovery of  
15 incentive compensation expense in Illinois also exists with respect to the AIP plan.  
16

17 **Q. At pages 8-9 of his rebuttal AAWC witness Townsley quotes from a West Virginia**  
18 **Public Service Commission decision where that commission had rejected an**  
19 **adjustment to remove the cost of incentive compensation. Please respond.**

20 A. Mr. Townsley is correct that the West Virginia declined to adjust West Virginia American  
21 Water Company's incentive compensation expense in that decision which was issued in  
22 March of 2009. He may not be aware, however, in view of the periods of economic  
23 hardship and high unemployment, in a subsequent order, the West Virginia commission  
24 continued to allow incentive compensation for utility employees, but rejected utility merit  
25 increases for non-officer salary positions and has found that it could not justify charging  
26 ratepayers for incentive compensation for senior management that was billed to a utility  
27 from its affiliated service company. In an Order dated November 30, 2009, the West

1 Virginia Commission stated at page 30, in a rate case decision involving Dominion Hope  
2 Gas, that:

3 Hope continued to advocate for merit increases for its non-officer salary  
4 employees for 2009, characterizing the \$84,099 as a known and measurable  
5 change. ...  
6

7 The Commission continues to view merit increases for non-officer salary positions  
8 as being questionable during periods of economic hardship and high  
9 unemployment. These salary increases, although known and reasonable, do not  
10 meet a prudence test given the financial conditions we are facing. With continuing  
11 financial turmoil in the national and global economy, the Commission rejects the  
12 necessity for ratepayers to bear this expense and excludes the adjustment Hope  
13 proposed.  
14

15 At page 31 of that decision, the West Virginia Commission allowed the incentive  
16 compensation for direct Hope employees; however, at pages 35-36, the affiliated service  
17 company charges for incentive compensation (and certain other affiliate expenses) were  
18 disallowed. Page 35 of that decision states in part as follows concerning the affiliate  
19 service company charges that were challenged:

20 14. DRS Charges

21 CAD and Staff challenged a number of expenses Hope included in its going level  
22 expenses that Dominion Resources Services, Inc. ("DRS"), the Dominion service  
23 company, billed to Hope. CAD recommended disallowing eight separate  
24 categories of DRS charges totaling \$364,570 in costs including (i) 50% of  
25 incentive compensation to senior management provided through DRS, (ii)  
26 membership dues, (iii) lobbying expenses, (iv) public relations expenses, (v)  
27 charitable contributions, (vi) social club dues, (vii) corporate sponsored sporting  
28 events, and (viii) \$134,979 in corporate aviation costs. .... CAD argued that the  
29 expenses, except for incentive compensation, are not required for providing gas  
30 service and do not benefit ratepayers. ... CAD split the incentive compensation  
31 charge as a reflection of the shared benefit of incentive compensation to both  
32 shareholders and ratepayers. Staff also recommended that the Commission  
33 eliminate a similar list of expenses (except for aviation charges) for a total of  
34 \$378,831. .... Staff asserted that Dominion stockholders benefit from these  
35 expenses and therefore should bear them. ...  
36

37 Hope objected to the CAD and Staff recommendations regarding the protested  
38 DRS charges. Hope argued that the incentive compensation charges from DRS are

1 a necessary part of the package Dominion uses to attract and retain talented  
2 executives. ...  
3

4 Page 36 of that decision presents the West Virginia Commission's conclusion on these  
5 issues as follows:

6 The Commission accepts the Staff recommendation regarding incentive  
7 compensation expenses for senior management charged by DRS to Hope. ... Hope  
8 has no senior management of its own and relies on DRS to provide those functions.  
9 While the Commission is sympathetic to the desires of Hope to attract and retain  
10 talented employees, **Hope executives should consider the current economic**  
11 **climate in their bonus requests.** As discussed above regarding merit increases  
12 for other salary employees, **the Commission cannot justify bonus costs for Hope**  
13 **executives in the midst of protracted economic turmoil.** The Commission  
14 disallows the DRS charges listed above removing \$378,831 Staff recommended  
15 plus \$134,979 in aviation costs for a total of \$513,810 from the cost of service  
16 calculations.  
17 (Emphasis supplied.)  
18

19 A copy of the pertinent excerpts from this decision is presented in Attachment RCS-8.  
20

21 **Q. Please summarize your recommendation concerning AAWC's incentive**  
22 **compensation expense.**

23 **A.** I recommend continuing the 30 percent allocation to shareholders ordered by the  
24 Commission in Decision No. 71410 for the incentive compensation expense for AAWC's  
25 own employees. This results in a reduction to test year expense of \$75,959, as  
26 summarized in the table below.

Summary of Adjustments to Achievement Incentive Pay

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (14,417)	\$ (18,690)	\$ (17,639)	\$ (10,772)	\$ (14,441)	\$ (75,959)

1           Additionally, I recommend a 100 percent disallowance for the incentive compensation  
2           charged to AAWC from affiliates as part of the affiliate Management Fee as shown in  
3           Schedule C-11 which is discussed in a subsequent section of my testimony relating to that  
4           adjustment.

5  
6   **C-4   Stock-Based Compensation Expense (All Districts)**

7   **Q.   Has AAWC agreed that stock-based compensation expense should be removed?**

8   A.   Yes. AAWC witnesses Broderick and Kiger's rebuttal testimony indicates that AAWC  
9       agrees that stock-based compensation expense should be removed.

10  
11   **Q.   Has stock-based compensation expense been disallowed by the Commission in rate**  
12       **cases for other utilities?**

13   A.   Yes. In Decision No. 69663, the Commission adopted Staff's recommendation that stock-  
14       based compensation be disallowed for Arizona Public Service Company ("APS").

15  
16   **Q.   Was stock-based compensation expense also disallowed in the Commission's decision**  
17       **in a rate case involving UNS Electric, Inc.?**

18   A.   Yes, it was. In Decision No. 70360 at page 22, the Commission, in referencing a similar  
19       decision regarding Southwest Gas Corporation as well as APS' last rate case stated:

20  
21               For these same reasons, we agree with Staff that test year expenses should  
22               be reduced to remove stock-based compensation to officers and  
23               employees...The disallowance of stock-based compensation is consistent  
24               with the most recent rate case for Arizona Public Service Company  
25               (Decision No. 69663).  
26  
27

1    **Q.    Was stock-based compensation expense removed by Staff in other recent utility rate**  
2       **cases?**

3    A.    Yes. Staff also removed the utility's stock-based compensation expense in the recent rate  
4       cases of Tucson Electric Power Company, Docket No. E-01933A-07-0402 and Southwest  
5       Gas Corporation, Docket No. G-01551A-07-0504.<sup>22</sup>

6  
7    **Q.    Please discuss the reasons for removing stock-based compensation.**

8    A.    Ratepayers should not be required to pay executive compensation that is based on the  
9       performance of the Company's (or its parent company's) stock price. Additionally, prior  
10      to being required to expense stock options for financial reporting purposes under  
11      Statement of Financial Accounting Standards No. 123 Revised (SFAS 123R), the cost of  
12      stock options was typically treated as a dilution of shareholders' investments, i.e., it was a  
13      cost borne by shareholders. While SFAS 123R now requires stock option cost to be  
14      expensed on a company's financial statements, this does not provide a reason for shifting  
15      the cost responsibility for stock options from shareholders to utility ratepayers.

16  
17   **Q.    Have you revised your adjustment to AAWC's Stock-Based Compensation?**

18   A.    Yes. As shown on Schedule C-4, using the corrected amounts identified in AAWC's  
19       rebuttal testimony, this adjustment decreases test year expense by \$83,041 to reflect the  
20       removal of AAWC's stock-based compensation for the AAWC districts in the current rate  
21       case. The expense of providing stock options and other stock-based compensation to

---

<sup>22</sup> Staff's adjustment to remove TEP's stock-based compensation was incorporated into a settlement approved by the Commission in Decision No. 70628. The ALJ's recommended opinion and order in Docket No. G-01551A-07-0504 adopted Staff's adjustment to remove stock-based compensation expense. The Commission's Decision No. 70665 in that case adopted the adjustment to remove expense for Southwest Gas's stock-based compensation expense.



officers and employees beyond their other compensation should be borne by shareholders and not by ratepayers.

**Q. What adjustment do you recommend for AAWC's stock-based compensation expense by district?**

**A.** As shown on Schedule C-4, expense for the AAWC districts in the current rate case is reduced by \$83,041. The adjustment by district is summarized in the table below.

Summary of Adjustments to Stock-Based Compensation

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (16,249)	\$ (21,178)	\$ (21,440)	\$ (13,094)	\$ (11,080)	\$ (83,041)

**C-5 Normalized Pension Expense (All Districts)**

**Q. What amount of pension expense has AAWC requested?**

**A.** In its initial filing, AAWC requested pension expense of \$2.090 million, before allocation among districts, based on funding payments into the defined benefit pension plan trust for 2009.

In its rebuttal filing, AAWC witness Kiger at pages 14-15 of his rebuttal is recommending an alternative that uses an average of 2009 and 2010 funding payments, which he identifies as \$2,090,643 and \$2,062,641, respectively.

**Q. Should these requests by AAWC for pension expense, based on amounts beyond the test year, be adopted?**

A. No. The pension expense requested by AAWC, which is based entirely on amounts beyond the test year, is abnormally high and should be rejected. In place of the substantially increased pension expense requested by AAWC, a normalized amount based on recent actual experience through the test year, should be used for ratemaking purposes.

**Q. How does the \$2.090 million pro forma amount used by AAWC for Pensions compare with the actual recorded expense in recent years?**

A. It is significantly higher than any amount for the last five years, 2004-2008, as shown in the following table:

**Comparison of Annual Pension Amounts**

		AAWC Request Exceeds	
Year	Amount	By Amount	Percent
Actual Recorded:			
2004	\$ 146,893 [a]	\$ 1,943,107	1322.8%
2005	\$ 317,798 [a]	\$ 1,772,202	557.7%
2006	\$ 1,013,141 [a]	\$ 1,076,859	106.3%
2007	\$ 903,222 [a]	\$ 1,186,778	131.4%
2008	\$ 1,734,561 [a]	\$ 355,439	20.5%
Averages:			
2004-2008	\$ 823,123	\$ 1,266,877	153.9%
2006-2008	\$ 1,216,975	\$ 873,025	71.7%
2007-2008	\$ 1,318,892	\$ 771,109	58.5%
AAWC Requested	\$ 2,090,000 [b]		
RUCO Normalized	\$ 1,318,892 [c]		

Notes and Source

[a] Annual recorded amounts from response to RUCO 2-60

[b] Company's requested amount is from AAWC Exhibit SLH-2 and is based upon 2009 funding contributions

[c] Based on two-year average, 2007-2008

The 2009 amount used by AAWC is abnormally high, and the unusually high amount appears to be driven by the poor stock market performance that occurred with the worldwide financial crises that began unfolding in the second half of 2008.

1 **Q. Do you have other concerns about AAWC's request for pension expense in this case?**

2 A. Yes, the amount requested by AAWC does not appear to have been based on its net  
3 periodic pension cost that is accrued pursuant to Statement of Financial Accounting  
4 Standards No. 87 ("FAS 87") but rather on a funding amount, which is subject to  
5 management discretion. As explained in response to RUCO 2-52, AAWC's requested  
6 pension expense "is based upon the funding requirement for the upcoming year based  
7 upon the actuarial report of Towers Perrin." A copy of that actuarial report was provided  
8 in response to RUCO 2-52.

9  
10 **Q. You mentioned FAS 87 as a measurement of pension expense. When was FAS 87**  
11 **promulgated and adopted for accounting purposes?**

12 A. FAS 87, Employer's Accounting for Pensions, was published in December 1985. For  
13 public companies, it was effective as required financial accounting for fiscal years  
14 beginning after December 15, 1986, and earlier application was encouraged. This is not a  
15 new accounting requirement. It has been applicable for financial accounting and reporting  
16 purposes now for 23 years.

17  
18 **Q. Do AAWC and its parent company American Water Works apply FAS 87?**

19 A. Yes. The American Water Works Company, Inc. ("AWWC") Securities and Exchange  
20 Commission ("SEC") Form 10-K for the period ending 12/31/2008 at page 127 shows Net  
21 periodic pension benefit cost for 2006, 2007 and 2008 of \$35.011 million, \$32.329 million  
22 and \$32.886 million, respectively.

23

1 Q. AAWC witness Broderick claims that AAWC uses an ERISA basis for pensions for  
2 ratemaking purposes. AAWC has also indicted in response to discovery that it has  
3 established a "regulatory asset" for differences between funding and FAS 87. What  
4 has AAWC provided to support its claim that Arizona is an "ERISA state" for  
5 pension and that AAWC has authorization to establish such a regulatory asset for  
6 the districts at issue in the current rate case?

7 A. Not much. AAWC's responses to discovery in the current rate case indicate that the  
8 Company is relying upon Decision No. 58419 for its justification for establishing a  
9 pension "regulatory asset"; however, Decision No. 58419 was issued in September 1993  
10 for Paradise Valley Water and thus applied to Paradise Valley and not to other utilities  
11 operating in Arizona that AAWC did not even own at that time. Moreover, Decision No.  
12 58419 reflected a Staff adjustment in that case to reduce Paradise Valley's requested  
13 pension expense by \$17,320 for the differences between FAS 87 and funded pension  
14 expense. At page 8, lines 9-16, that Decision stated that:

15  
16 In its rebuttal testimony, the Company agreed to Staff's pro forma  
17 adjustment on the condition that the Commission allow the Company to  
18 establish and maintain a regulatory asset for SFAS 87 costs.

19 We agree that it is appropriate to exclude the \$17,320 and that the  
20 Company should establish a deferral account as a result of its  
21 implementation of SFAS 87, for possible recovery in a future rate  
22 application.  
23

24 In summary, \$17,230 was excluded and Decision No. 58419 states that "the Company  
25 should establish a deferral account as a result of its implementation of SFAS 87, for  
26 possible recovery in a future rate application." This says "possible" recovery, not  
27 "probable" recovery, which is often cited as one of the criteria for establishing a  
28 regulatory asset under FAS 71. At page 8, Decision No. 58419 says that Paradise Valley

1       should establish a "deferral account" not a "regulatory asset" account. To accountants,  
2       there is a difference between a mere "deferral account" and a regulatory asset. Also, there  
3       is nothing in the "Findings of Fact" on pages 19-21, or the "Order" provisions at pages 21-  
4       23 of Decision No. 58419 that instruct Paradise Valley to establish a regulatory asset for  
5       pension-based differences. In sum, AAWC's apparent heavy reliance upon Decision No.  
6       58419 as authorizing a "regulatory asset" for pensions, even for Paradise Valley Water  
7       Company, may have been misplaced.

8               Moreover, Decision No. 58419 applied only to Paradise Valley Water, not to other  
9       water utility operations acquired by American Water after 1993.

10              The Company's response to RUCO 7-1(c) also states that "AAWC continues to  
11       debit a regulatory asset for the on-going difference between pension accruals and  
12       contributions." Yet, also according to the Company's response to RUCO 7-1(c), AAWC  
13       has stated that the issue has not been revisited since the ACC's 1993 Decision No. 58419.  
14       It could be irresponsible on the part of a utility to not raise the issue of recovery of a  
15       substantially growing deferral amount in each subsequent rate case, especially when the  
16       amount of cost deferral being recorded (perhaps without adequate authorization) as a  
17       "regulatory asset" was growing over a hundred fold.

18              The Company's apparent failure to notify the Commission of a growing and now  
19       apparently multi-million dollar sized pension "regulatory asset" that is now orders of  
20       magnitude higher than the \$17,230 amount that was specifically mentioned in Decision  
21       No. 58419 and the Company's apparent failure to bring the pension "regulatory asset"  
22       issue to the Commission's attention for deferral authorization subsequently to that 1993

1 case may thus have created or contributed to accounting and regulatory problems for  
2 AAWC.

3  
4 **Q. At pages 13-14 of his rebuttal testimony, AAWC witness Broderick requests that, if**  
5 **the Commission decides to approve FAS 87 based pension expense in this case,**  
6 **AAWC wants to charge ratepayers for prior differences between FAS 87 and**  
7 **ERISA, based on amounts that AAWC has deferred in accounts 186408 and 186422**  
8 **over a five-year period. Should that AAWC request be adopted?**

9 **A.** No. To date, other than citing Decision No. 58419, which did not authorize a regulatory  
10 asset, and which applied to Paradise Valley, not to any of the districts at issue in the  
11 current AAWC rate case, AAWC has provided nothing of reliable substance that would  
12 justify charging ratepayers of any of the AAWC utilities in the current rate case for a  
13 multi-million dollar pension "regulatory asset" that was apparently never clearly presented  
14 by AAWC to the Commission or authorized by the Commission for the specific water and  
15 wastewater utilities whose revenue requirements are at issue in the current AAWC rate  
16 case. This request by AAWC for amortization of a pension "regulatory asset" should be  
17 rejected. In addition to being inappropriate and apparently without proper Commission  
18 authorization with respect to the deferral, such an amortization in the current case would  
19 exacerbate even further the shockingly high pension expense increases that the Company  
20 is requesting.

21

1 Q. At page 10 of his rebuttal, Mr. Broderick states that: "The Company believes that  
2 Mr. Smith has greatly exaggerated the 'management discretion' associated with  
3 ERISA expense." Please respond.

4 A. Management has wide discretion when it comes to plan funding and plan design. As an  
5 example, AWWC closed its pension plan for any employees hired on or after January 1,  
6 2006. Union employees hired on or after January 1, 2001 had their accrued benefits frozen  
7 and will be able to receive this benefit as a lump sum upon termination or retirement.  
8 Union employees hired on or after January 1, 2001 and non-union employees hired after  
9 January 1, 2006 are provide with a 5.25 percent of base pay defined contribution plan.  
10 Additionally, as part of the RWE divestiture the management and shareholders could have  
11 determined to leave the AWWC defined benefit pension plan in a fully funded status,  
12 making it less vulnerable prospectively to investment declines.

13  
14 Q. Has the parent company, AWWC, already put its shareholders on notice that the  
15 disruption in the capital markets adversely affects the value of the investments held  
16 within AWWC's employee benefit plans, and this can adversely affect AWWC's  
17 results of operations, including shareholders' equity?

18 A. Yes. In AWWC's 2008 SEC Form 10-K (filed 2/27/09) at page 28, investors have been  
19 put on notice by AWWC that the:

20 **The disruption in the capital markets and its actual or perceived effects on**  
21 **particular businesses and the greater economy also adversely affects the value of**  
22 **the investments held within the Company's employee benefit plan trusts.**  
23 **Significant declines in the value of the investments held within the Company's**  
24 **employee benefit plant trusts may require the Company to increase**  
25 **contributions to those trusts in order to meet future funding requirements if**  
26 **the actual asset returns do not recover these declines in value in the**  
27 **foreseeable future. These trends may also adversely impact the Company's**

1 results of operations, net cash flows and financial positions, including our  
2 shareholder's equity.  
3 (Emphasis supplied.)  
4

5 Q. What else does the AWWC 2008 SEC Form 10-K state on page 28 with respect to the  
6 impact the disruption of capital markets had on the value of its benefit plan assets?

7 A. It describes how the poor investment market conditions can unfavorably impact the value  
8 of AWWC's benefit plan assets, which could then require significant additional funding:

9 **Market conditions may unfavorably impact the value of benefit plan assets**  
10 **and liabilities which then could require significant additional funding.**  
11 The performance of the capital markets affects the values of the assets that are held  
12 in trust to satisfy future obligations under the Company's pension and  
13 postretirement benefit plans and could significantly impact our results of  
14 operations and financial position. The Company has significant obligations in these  
15 areas and the Company holds significant assets in these trusts. These assets are  
16 subject to market fluctuations, which may affect investment returns, which may  
17 fall below the Company's projected return rates. **A decline in the market value of**  
18 **the pension and postretirement benefit plan assets, as was experienced in**  
19 **2008, will increase the funding requirements under the Company's pension**  
20 **and postretirement benefit plans if the actual asset returns do not recover**  
21 **these declines in value.** Additionally, the Company's pension and postretirement  
22 benefit plan liabilities are sensitive to changes in interest rates. As interest rates  
23 decrease, the liabilities increase, potentially increasing benefit expense and funding  
24 requirements. Further, changes in demographics, including increased numbers of  
25 retirements or changes in life expectancy assumptions may also increase the  
26 funding requirements of the obligations related to the pension and other  
27 postretirement benefit plans. Also, **future increases in pension and other**  
28 **postretirement costs as a result of reduced plan assets may not be fully**  
29 **recoverable from our customers,** and our the results of operations and financial  
30 position of the Company could be negatively affected.  
31

32 **During 2008, the Company's unfunded status of its pension plan increased**  
33 **significantly primarily due to lower than expected 2008 asset returns, which**  
34 **are expected to result in increased benefit costs and required funding**  
35 **contributions in future years.** Based on current plan assets and expected future  
36 asset returns, the Company currently estimates the increase to pension and  
37 postretirement expense (net of capitalized amounts) in 2009 to be approximately  
38 \$32 million, pre-tax. It is the Company's intent to work with PUCs in the states in  
39 which it operates to minimize the impact of such increases on its results of  
40 operations. The Company currently expects to make pension and postretirement



1 benefit contributions to the plan trusts of \$125.9 million, \$132.5 million, \$124.7  
2 million, \$161.9 million and \$123.2 million in 2009, 2010, 2011, 2012 and 2013  
3 respectively. Actual amounts contributed could change significantly from these  
4 estimates  
5 (Emphasis supplied.)

6  
7 As indicated above, AWWC has already put its shareholders on notice that **“increases in**  
8 **pension and other postretirement costs as a result of reduced plan assets may not be**  
9 **fully recoverable from our customers.”** This notice by the parent company, AWWC, to  
10 its shareholders, is consistent with a ratemaking treatment that holds shareholders  
11 responsible for extraordinarily high pension costs that have been caused by the capital  
12 market disruptions and worldwide financial crisis.

13  
14 **Q. Do you agree with AAWC witness Kiger’s claim at page 14, lines 10-11, that “it is**  
15 **essential that the Company recover its actual pension and OPEB expense”?**

16 **A.** No. It is not essential that AAWC recover or that its ratepayers (many of whom are also  
17 suffering from the economic disruptions) bear, an abnormal level of pension (or OPEB)  
18 expense, especially when the level of pension expense being requested by the Company  
19 has increased so significantly because of capital market disruptions and abnormally poor  
20 investment market performance. What is essential is that the Commission balance the  
21 interests of ratepayers and shareholders, and, where necessary, hold shareholders  
22 responsible for unusual and abnormal cost increases. AAWC’s request for 2009 or even  
23 an average of 2009 or 2010 pension expense should be rejected. There is no requirement  
24 that a utility like AAWC be allowed to recover “actual” expenses for pensions or other

1 items when those expenses are at abnormal levels due to unprecedented capital market  
2 disruptions and where the utility's requested amounts are for periods beyond the test year.

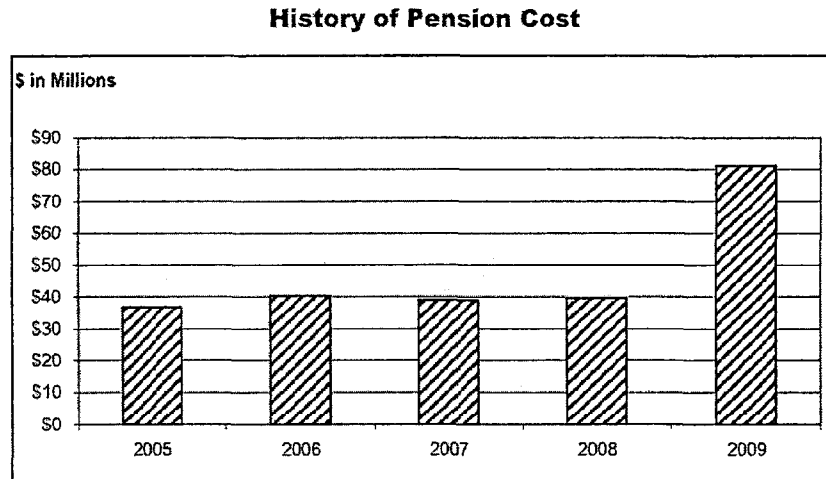
3  
4 **Q. Should AAWC's ratepayers be held responsible for the impact of the temporary**  
5 **poor market conditions that caused a significant decline in the AWWC benefit plan**  
6 **assets by having to pay pension expense that is abnormally high as a result of the**  
7 **disruption of capital markets and its impact on the value of its benefit plan assets?**

8 A. No. Ratepayers should be responsible only for paying for a reasonable and normal  
9 amount of pension expense. The large increases in AAWC's pension expense reflected in  
10 AAWC's proposal to use post-test year amounts should be rejected. Ratepayers, who are  
11 also suffering from the challenging economic conditions, should not be held responsible  
12 for substantially increased pension expense that resulted from the disruption of capital  
13 markets and its impact on the value of the AWWC benefit plan assets. It was the  
14 Company's (and the parent company, AWWC,) management that designed the benefit  
15 plan and utilizes discretion concerning the funding amount (AWWC has apparently  
16 decided to fund only the minimum required amount), and thus which has exposed the  
17 Company to the volatility in this expense that has been impacted by the disruption of  
18 capital markets.

19  
20 **Q. What does the Company's actuarial report show for the FAS 87 Pension Cost**  
21 **amount and how does it compare with prior years?**

22 A. The FAS 87 pension cost for January 1, 2009 for AWWC is listed on page MS-2 of the  
23 report and is \$81,116,478. The 2009 expense is much higher than in previous years as

shown in the "History of Pension Cost" tables from page MS-4 of the report, which are reproduced for ease of reference below:



The following table shows the relative dollar amounts in total and the percent of covered pay:

<b>History of Pension Cost</b>			
-----Pension cost-----			
<i>Fiscal year</i>	<i>Amount</i>	<i>Percent of covered pay</i>	<i>Discount rate</i>
2009*	\$ 81,116,478	26.1%	6.12%
2008*	39,625,996	13.4	6.27
2007*	38,968,697	13.5	5.90
2006	40,327,960	16.7	5.65
2005	36,845,672	15.5	6.00

\* All values on or after 2007 reflect the merger of Elizabethtown Water Company Pension Plan as of December 31, 2006.

As can be seen, the total cost for 2009 has more than doubled the cost of any of the prior years, 2005 through 2008. Additionally, the cost as a "percent of covered pay" at 26.1 percent for 2009 is also almost double the 13.4 percent and 13.5 percent for the prior years

2008 and 2007, respectively. As shown on page SI-3 of the actual report, the dollar cost per active participant is \$16,626 for fiscal 2009, which is more than double the comparable amount of \$7,842 for fiscal 2008.

**Q. Does the actuarial report show how the pension cost under FAS 87 changed from 2008 to 2009?**

**A.** Yes. This is shown at page MS-2, and summarized in the following table:

**Change in Pension Cost and Overfunded (Underfunded) PBO**

The pension cost increased from \$39,625,996 in fiscal 2008 to \$81,116,478 in fiscal 2009 and the underfunded PBO increased from \$(265,135,065) on January 1, 2008 to \$(479,814,107), as set forth below:

	<b>Pension Cost</b>	<b>Funded Position</b>
Prior year	\$ 39,625,996	\$ (265,135,065)
Change due to:		
▶ Expected based on prior valuation	(2,982,015)	42,493,168
▶ Loss (gain) from noninvestment experience	1,762,793	(16,002,728)
▶ Loss (gain) from asset experience	37,809,962	(209,099,734)
▶ Assumption changes	4,899,742	(32,069,748)
▶ Plan amendments	<u>0</u>	<u>0</u>
Current year	\$ 81,116,478	\$ (479,814,107)

As can be seen, there was a loss on the assets of over \$209 million which resulted in an increase to the pension cost of approximately \$37.8 million. Page MS-3 of the report lists the following as "significant reasons" for the changes:

- The return on the fair value of plan assets since the prior measurement date was less than expected, which increased the underfunded PBO and increased pension cost.
- The assumed rate of future salary increases was lowered by 25 basis points, which decreased pension cost and decreased the underfunded PBO.

- 1 • The overtime assumption for union participants and nonunion, nonexempt participants
- 2 was increased, which increased the underfunded PBO and decreased pension cost.
- 3 • The discount rate for benefit obligations was changed from 6.27% to 6.12%, which
- 4 increased pension cost and increased underfunded PBO.
- 5 • Minor losses from what was assumed for plan demographics occurred, which
- 6 increased pension cost and increased underfunded PBO.
- 7

8 As described on page SI-1 of the actuarial report, the plan experienced a rate of return of  
9 negative 24.6 percent in 2008, and had an investment return of negative \$160 million.  
10 This compares with a negative investment return of \$41.9 million in 2007, which equated  
11 to a negative return of approximately 6.6 percent. A copy of that actuarial report was  
12 included with my direct testimony in Attachment RCS-4.

13  
14 **Q. You mentioned that the return on the AWWC defined benefit pension plan assets**  
15 **was a negative 24.6 percent in 2008, which contributed to the abnormally high**  
16 **pension expense that AAWC is seeking. Did the Company provide the return on**  
17 **pension plan assets for 2009?**

18 **A. Yes. The Company's response to RUCO 2-95 states that, "the total return year-to-date**  
19 **2009 is 20.34%."**

20  
21 **Q. Does the actuarial report describe AAWC's funding policy for its defined benefit**  
22 **pension plan?**

23 **A. Yes. This is discussed at page MS-6, as follows:**

24 American Water's funding policy is to contribute an amount equal to the  
25 minimum required contribution under ERISA. American Water may  
26 increase its contribution above the minimum if appropriate to its tax and  
27 cash position and the plan's funded position. American Water makes plan  
28 contributions each plan year in four installments, one in August, one in

1 November, one in February, and one in May, which, in total, suffice to  
2 cover the minimum funding requirement for the plan year, and, individually,  
3 suffice to cover the quarterly requirements in October, January, April, and  
4 July respectively of each plan year.  
5

6 Plan year contributions were made in the amounts of \$15,000,000 during  
7 August of 2008, \$15,000,000 during November of 2008, and \$17,100,000  
8 during February of 2009. Additionally, \$17,100,000 is expected to be  
9 funded during May of 2009.  
10

11 **Q. Are the funding contributions discretionary with management?**

12 A. Yes. Within limits, the funding contributions for a defined benefit pension plan are  
13 discretionary with AWWC management.  
14

15 **Q. What are the limits based upon?**

16 A. The limits typically involve looking at three areas:

17 (1) the minimum required contribution under ERISA;

18 (2) the contribution needed to meet the funding target under the Pension Protection Act of  
19 2006 ("PPA"); and

20 (3) the maximum tax deductible contribution.

21 The ERISA and PPA analysis is sometimes used to establish the minimum amount of  
22 annual funding. Frequently, there can be an extremely wide range between some of these  
23 measures. For example, as described in the actuarial report on pages MS-5 and MS-6, the  
24 estimated maximum tax deductible contribution was \$737.3 million and the minimum  
25 funding requirement under the PPA was approximately \$64.2 million. These figures for  
26 the plan year beginning July 1, 2008 are also shown on pages SI-6 and SI-8, along with  
27 comparative information from the prior year. The difference between the maximum tax  
28 deductible contribution of \$737.3 million and the minimum required contribution of \$64.2

1 million is over \$673 million, and the amount to choose to contribute to the defined benefit  
2 plan trust within this range is up to management discretion.

3  
4 **Q. What do you recommend for pension expense in the current case?**

5 A. I recommend using a two-year average of the FAS 87 amounts for pension expense to  
6 establish a normalized level for AAWC in the current case. The use of an average is  
7 needed because the 2009 results are abnormally high and reflect a FAS 87 amount that  
8 almost doubled the 2007 and 2008 experience, largely due to the poor investment returns  
9 experienced by the AWWC pension trust in the latter part of 2008 and early 2009.

10  
11 **Q. Is it widely accepted to use the FAS 87 amounts for establishing pension expense in**  
12 **utility ratemaking proceedings?**

13 A. Based on my experience, yes it is. Regulatory commissions typically either base pension  
14 expense upon the FAS 87 accruals, or use the cash funding contributions. Because the  
15 range of potential cash funding contributions has become so wide in recent years, and is  
16 subject to such a degree of management discretion, I believe it is better to base the  
17 ratemaking allowance for pension expense on the FAS 87 results, normalized to remove  
18 the abnormal results that affected the AWWC defined benefit plan for 2009.

19  
20 **Q. How does your recommendation for a normalized level of pension cost compare with**  
21 **prior years, and with AAWC's request, in terms of a cost per participant and**  
22 **percent of covered pay?**

23 A. These comparisons are presented in the following tables:

Pension Cost Per Active Participant and As Percent of Covered Pay			
Period	Per Active Participant	Percent of Covered Pay	Notes/ Source
Fiscal 2006	\$ 8,836	16.70%	[a]
Fiscal 2007	\$ 7,700	13.50%	[a]
Fiscal 2008	\$ 7,842	13.40%	[a]
Fiscal 2009	\$ 16,626	26.10%	[a]
RUCO Normalized	\$ 11,374	14.50%	[b]
AAWC Requested	\$ 19,539	24.90%	[c]
Notes/Source			
[a] Per AWWC actuarial reports, May 2007 and March 2009			
[b] RUCO adjustment, percent of covered pay estimated			
[c] AAWC adjustment, percent of covered pay estimated			

1  
2  
3 **Q. Has the parent company, AWWC, closed its defined benefit plan to new employees?**

4 **A.** Yes. In general, employees hired or rehired after January 1, 2006 are not eligible to  
5 participate in the AWWC defined benefit pension plan.<sup>23</sup>

6  
7 **Q. Did you describe in your direct testimony how closing or limiting participation in**  
8 **defined benefit pension plans appears to be consistent with an overall trend?**

9 **A.** Yes. For example, in my direct testimony I referenced a report issued in March 2009 by  
10 the U.S. Government Accountability Office (GAO-09-291)<sup>24</sup>, which concluded, among  
11 other things, that the number of private defined benefit (DB) pension plans has declined  
12 substantially over the past two decades. For example, about 92,000 single-employer DB  
13 plans existed in 1990, compared to just under 29,000 single-employer plans today.  
14 Additionally, there is a widespread concern that large DB plans covering many  
15 participants have modified, reduced, or otherwise frozen plan benefits in recent years.

<sup>23</sup> Details of eligibility are described in the March 2009 actuarial report at page SI-23, including certain exceptions for certain union groups.

<sup>24</sup> A copy of the complete GAO study can be obtained online at: <http://www.gao.gov/new.items/d09291.pdf>



1 The GAO's survey results also suggest that the long-time stability of larger DB plans is  
2 now vulnerable to the broader trends of eroding retirement security, and noted that the  
3 market turmoil recently experienced appears likely to exacerbate this trend.

4  
5 **Q. What type of pension plan does AWWC offer to employees hired after January 1,**  
6 **2006?**

7 A. The Company's pension expense workpaper states: "Beginning 1/1/06, the Company no  
8 longer offers a Pension Plan to new hires. Instead, new hires get the Defined Contribution  
9 Plan as a benefit. The Company will contribute 5.25% of Base Pay into a Defined  
10 Contribution Plan."

11  
12 **Q. How does the cost of the Defined Contribution Plan compare with the cost of the**  
13 **Defined Benefit plan?**

14 A. The cost comparison is shown in the following table:

Average Cost Per Active Participant				
As Adjusted	AWWC Defined Benefit Plan	Defined Contribution Plan	Excess Cost for Defined Benefit	Percent Excess for DB Plan
RUCO Normalized	\$ 11,374	\$ 2,628	\$ 8,746	333%
AAWC Requested	\$ 19,539	\$ 2,628	\$ 16,911	643%
Source: Pension adjustment workpaper				

15  
16 As can be seen, the defined benefit plan is substantially more costly on a "per active  
17 participant" basis.

18  
19 **Q. Are you recommending any adjustment for the expense related to AAWC's Defined**  
20 **Contribution Plan?**

1 A. No.

2  
3 **Q. Does RUCO Adjustment C-5 cover pension costs that are charged to AAWC from**  
4 **affiliated companies via the Management Fee?**

5 A. No. RUCO Adjustment C-5 addresses the amount of normalized pension expense for  
6 AAWC employees. There are significant additional charges to AAWC from the affiliated  
7 Management Fee which include charges for pensions as well as numerous other expenses.  
8 The affiliated charges to AAWC from the Management Fee, including the affiliated  
9 charges for pensions, are addressed in a subsequent section of my testimony.

10  
11 **Q. What specific adjustment do you recommend?**

12 A. I recommend an adjustment to decrease the Company's requested amount of pension  
13 expense by \$280,339 as shown on Attachment RCS-6 and RCS-7, Schedule C-5. The  
14 amount of pension expense requested by AAWC for each district should be reduced by the  
15 amounts listed below:

Summary of Adjustments to Pension Expense

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (39,203)	\$ (92,636)	\$ (72,483)	\$ (25,187)	\$ (50,830)	\$ (280,339)

16  
17  
18 **Q. Please explain the calculations on Schedule C-5.**

19 A. The Company provided actual AAWC recorded pension expense for prior years in  
20 response to RUCO 2-60. I have used the average of 2007 through 2008 as the basis for a  
21 normalized pension expense allowance. I have replaced the \$2,090,643 abnormally high

1 2009 result that AAWC used with the \$1,318,892 normalized amount, and ran this  
2 through the Company's detailed Excel file [AZ 2008 Labor Pension Adjustment.xls] to  
3 derive an adjustment to decrease the Company's requested pension expense by \$280,339  
4 for all of the districts in the current case combined. Schedule C-5 shows the amount of  
5 adjustment for each of the five districts in this proceeding. Schedule C-5.1, which consists  
6 of two pages, reflects the results from using the recommended allowable level, based on  
7 the three-year average to determine the normalized amount.

8  
9 **Q. Have you modified this recommendation as the result of AAWC's rebuttal**  
10 **testimony?**

11 **A.** No. Instead of modifying its large pension increase that was reflected in its direct filing,  
12 AAWC's rebuttal testimony attempts to increase pension expense even more. At page 16  
13 of AAWC witness Kiger's rebuttal testimony AAWC attempts to increase pension  
14 expense by an additional \$72,296 for the five districts for affiliated pension expense. I  
15 comment briefly on this AAWC proposal in conjunction with Adjustment C-12, discussed  
16 below in my surrebuttal testimony.

17  
18 **Company's Request to Defer Pension Expense**

19 **Q. AAWC witness Broderick's rebuttal testimony at page 13 cites a request made by**  
20 **AAWC for approval to defer \$1.723 million in 2009 pension expense and to continue**  
21 **such deferral through December 31, 2013. Should such a deferral be permitted?**

22 **A.** No. This AAWC request is apparently pending in another Docket (09-0241); however,  
23 this is directly related to a major issue in the current AAWC rate case – determining a

1 reasonable and normal allowance for pension expense for ratemaking purposes. The  
2 Company's position that it should be allowed to charge ratepayers for every dollar of its  
3 "actual" or "exact"<sup>25</sup> pension expense, even when such expense is abnormally high as the  
4 result of unprecedented capital market disruptions, should be rejected. No deferrals of  
5 2009 pension expense should be permitted. The Company's requested double-digit rate  
6 increases are bad enough without placing additional burdens on ratepayers to pay  
7 additional amounts in subsequent AAWC rate cases for deferrals of abnormally high 2009  
8 pension expense. The Company's request for single issue ratemaking via "a balancing  
9 account feature" for "exact" recovery of pension expense in periods not corresponding to a  
10 rate case test year should be rejected.

11  
12 **Company's Request to Charge Ratepayers for an Amortization of a Pension "Regulatory**  
13 **Asset"**

14 **Q. Please address the requests made at pages 13-15 of AAWC witness Broderick's**  
15 **rebuttal testimony for additional charges to ratepayers for amortization and rate**  
16 **base inclusion of differences that AAWC deferred on its books for the difference**  
17 **between FAS 87 and ERISA-funded amounts for pensions.**

18 **A. At pages 13-15 of his rebuttal testimony AAWC witness Broderick requests that AAWC**  
19 **be allowed to charge ratepayers for deferrals AAWC has recorded on its books in**  
20 **Accounts 186408 and 186422, which he states total \$746,347 and \$1,050,173 as of**  
21 **February 28, 2010, and for a five-year amortization of such amounts (which AAWC**  
22 **apparently wants to update even further beyond the 2008 test year), and for inclusion in**

---

<sup>25</sup> See, e.g., Broderick rebuttal, page 13, lines 8-9 "the Company would only recover its exact pension expense" and  
11 "it is only seeking to recover its exact pension expense."

1 rate base of the unamortized balances. There are several problems and concerns with  
2 regard to this AAWC request. First, AAWC has not demonstrated that it ever requested or  
3 received Commission authorization to record such deferrals for any of the districts at issue  
4 in the current AAWC rate case. The only thing AAWC has been able to point to as  
5 potentially authorizing a deferral is Decision No. 58419, which only addressed a minimal  
6 deferral for Paradise Valley. I discussed that Decision above.

7 Additionally, there is an element of retroactive ratemaking in AAWC's proposal.  
8 For AAWC to have assumed that it could defer differences between FAS 87 and ERISA  
9 without obtaining specific Commission authorization for such deferrals is questionable at  
10 best. If the deferrals that AAWC recorded were not specifically authorized by the  
11 Commission, the amounts should be written off. From the documentation provided to date  
12 by AAWC, it appears the Company has not cited adequate authorization for such deferrals  
13 for the districts in the current AAWC rate case, and it was therefore questionable at best  
14 for such amounts to have been deferred on AAWC's books. As noted above, FAS 87 has  
15 been in existence for over 20 years.

16 Finally, the total amount of pension expense being included in rates should be  
17 reviewed for reasonableness and adjusted to a reasonable and normal level. AAWC's  
18 initially filed request, which was based on a 2009 amount that had been impacted by  
19 unprecedented disruptions in the capital markets, is too high and is based on abnormal  
20 conditions, and should therefore be adjusted downward using a historical average as I  
21 have recommended. Loading additional pension expenses into the 2008 test year based on  
22 questionable prior deferrals, and inclusion of such deferral balances in rate base as  
23 requested by AAWC is not appropriate and should be rejected.

**C-6 Normalized Other Post Employment Benefits Expense (All Districts)**

**Q. What amount of Other Post Employment Benefits ("OPEB") expense has AAWC used?**

A. As shown on Company Exhibit SLH-14, AAWC has used an OPEB expense of \$95,763, before allocation among AAWC districts and reduced it by a capitalization rate of 18.3 percent, to derive its proposed expense of \$78,238.

**Q. How does the \$95,763 pro forma amount used by AAWC for OPEBs compare with the actual recorded expense in recent years?**

A. It is significantly higher than any amount for the last five years, 2004-2008, as shown in the following table:

**Comparison of Annual OPEB Amounts**

		AAWC Request Exceeds	
Year	Amount	By Amount	Percent
Actual Recorded:			
2004	\$ 73,823 [a]	\$ 21,940	29.7%
2005	\$ 63,196 [a]	\$ 32,567	51.5%
2006	\$ 74,032 [a]	\$ 21,731	29.4%
2007	\$ 62,603 [a]	\$ 33,160	53.0%
2008	\$ 75,723 [a]	\$ 20,040	26.5%
Averages:			
2004-2008	\$ 69,875	\$ 25,888	37.0%
2006-2008	\$ 70,786	\$ 24,977	35.3%
2007-2008	\$ 69,163	\$ 26,600	38.5%
AAWC Requested	\$ 95,763 [b]		
RUCO Normalized	\$ 69,163 [c]		

**Notes and Source**

[a] Annual recorded amounts from response to RUCO 2-60

[b] Company's requested amount is from AAWC Exhibit SLH-14

[c] Based on two-year average, 2007-2008

1 **Q. Please explain RUCO Adjustment C-6.**

2 A. This adjustment is shown on Schedule C-6 of Attachments RCS-6 and RCS-7 for water  
3 and wastewater districts, respectively. This adjustment normalizes the OPEB expense,  
4 using an average of 2007-2008 as the basis for deriving a normal level for ratemaking  
5 purposes. This adjustment reduces the \$95,763 amount used by AAWC to \$69,163,  
6 before capitalization, and reduces the OPEB expense from \$78,238 to \$56,529, after  
7 capitalization. The adjustment for each of the districts by the amounts is shown on  
8 Schedule C-6 of Attachments RCS-6 and RCS-7. For all of the districts included in the  
9 current rate case filing, the adjustment decreases OPEB expense by \$10,389. The  
10 reduction to each district is shown in the following table:

Summary of Adjustments to OPEB Expense

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (2,033)	\$ (2,650)	\$ (2,682)	\$ (1,638)	\$ (1,386)	\$ (10,389)

11  
12  
13 **Q. Have you adjusted this adjustment based on AAWC's rebuttal testimony?**

14 A. No. This adjustment is appropriate to provide for a reasonable amount of OPEB expense.  
15 While not nearly as egregious as the pension expense situation discussed above, AAWC's  
16 request for OPEB expense is also based on 2009 information (i.e., is beyond the 2008 test  
17 year) and was apparently also impacted by the abnormal investment market conditions. A  
18 downward adjustment of \$10,389 to AAWC's request for OPEB expense is therefore  
19 appropriate.  
20

**C-7 Donations, Membership Dues, Advertising and Miscellaneous (All Districts)**

**Q. Please explain RUCO Adjustment C-7.**

A. This adjustment removes expenses for donations, membership dues, certain advertising expense, and miscellaneous expenses. These costs, which were identified from AAWC's response to RUCO 2-43, are discretionary and not needed for the provision of safe and reliable utility service. The adjustment to remove expenses not typically recovered from customers in the current rate case is shown on Attachment RCS-6, Schedule C-7, and summarized in the following table:

Summary of Adjustments to Dues, Donations & Misc. Expense

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (3,250)	\$ (4,237)	\$ (4,289)	\$ (2,620)	\$ (2,216)	\$ (16,612)

**Q. Has this adjustment been revised for anything in AAWC's rebuttal testimony?**

A. No.

**Q. Has AAWC accepted this adjustment?**

A. Yes. AAWC witness Kiger's rebuttal testimony at page 11 indicated that AAWC has accepted this adjustment.

**C-8 Tank Maintenance Reserve Fund Accrual (Sun City Water and Anthem Water)**

**Q. What has AAWC requested for a Tank Maintenance Reserve Fund Accrual?**

A. AAWC is requesting an additional expense for Sun City Water of \$445,000 annually for a Tank Maintenance Reserve Fund Accrual, as shown on Company Schedule C-2, page 29.



1                   In Mr. Broderick's' rebuttal testimony at page 10, AAWC is now apparently also  
2 requesting that a tank painting and inspections deferral be approved for Anthem Water  
3 District.  
4

5   **Q.     What is a Reserve Fund Accrual?**

6   A.    A Reserve Fund Accrual typically involves charging (increasing) an Expense and  
7 crediting (increasing) a Liability (or Accrued Reserve) account. It essentially charges an  
8 expense before the expense is incurred. The accumulated expense accruals are recorded in  
9 the Liability (or Reserve) account, which would thus represent an additional source of  
10 ratepayer-provided cost-free capital to the utility. When actual expenses are paid, the  
11 Liability (or Reserve) account would be reduced.  
12

13   **Q.     How is a Reserve Fund Accrual different from recording expenses as they are**  
14 **incurred?**

15   A.    Recording expenses as they are incurred typically involves crediting Cash or Accounts  
16 Payable and debiting (charging) an Expense when a cost is actually incurred. In contrast,  
17 charges to expense for a Reserve Accrual records the expense before it is incurred. The  
18 use of a Reserve Accrual essentially results in ratepayers pre-paying for the expense.  
19 Also, because of the operation of the Reserve account, this also contains undesirable  
20 elements of single-issue ratemaking, where a specific expense item, in this case Tank  
21 Painting, is singled out from all of the utility's other expenses, and essentially gets tracked  
22 (in the Accrued Reserve Account) for dollar-for-dollar recovery. As such, unless there is  
23 a very compelling reason for establishing a Reserve Fund Accrual, this single-issue

1 approach to utility regulation is undesirable, and has the impact of shifting responsibility  
2 of fluctuations in the expense between rate cases away from the utility and onto  
3 ratepayers. AAWC's Reserve Accrual embodies these undesirable features and requires  
4 ratepayers to pre-pay for expenses before they are incurred by the utility. That AAWC  
5 proposal should therefore be rejected.

6  
7 **1. Sun City Water Tank Maintenance Reserve Fund Accrual**

8 **Q. Why should AAWC's requested Tank Maintenance Reserve Fund Accrual for Sun**  
9 **City Water be rejected?**

10 **A.** AAWC's tank painting reserve for Sun City Water would have ratepayers paying for tank  
11 painting before the money is expended on tank painting. There is no need for ratepayers  
12 to pre-fund tank painting expense.

13 Additionally, with the large percentage rate increases being requested by AAWC  
14 and the poor economy, this seems like a particularly bad time to start forcing ratepayers to  
15 pre-pay for expenses that the utility has not yet incurred.

16 Establishing ratepayer pre-funding for a Reserve account also has elements of  
17 single issue ratemaking. There is no compelling need to single out tank painting expense  
18 for special ratemaking treatment. A normalized allowance for tank painting expense can  
19 be reflected in rates based on an average of recent actual experience through the test year,  
20 if the test year amount itself were to be viewed as being abnormal. Establishing a  
21 Reserve, on the other hand, would remove incentives to control the expense between rate  
22 cases, and would virtually guarantee dollar for dollar recovery by the utility of such  
23 expenditures.

Moreover, there is not much, if any, difference in the Tank Maintenance Reserve Fund Accrual that AAWC is requesting in the current rate case and the one recently proposed by AAWC in its last rate case, which was rejected by the Commission. The Commission recently rejected a similar proposal by AAWC in Docket Nos. W-01303A-08-0227 et al. which would apparently have applied for all of the water districts for which AAWC had sought rate increases in that case.

**Q. Please discuss the "Tank Maintenance Reserve" issue from Docket Nos. W-01303A-08-0227 et al.**

**A.** Decision No. 71410 discusses this issue at pages 36-37. At page 36, Decision No. 71410 describes the AAWC proposal as follows:

The Company proposed a reserve for water tank maintenance expense which would provide an annual allowance for tank maintenance costs in operating expenses. Under the Company's proposal, the funds collected through rates would be recorded in a deferred liability account labeled Reserve for Tank Maintenance, and the Reserve for Tank Maintenance account would be charged as tank maintenance expenses are incurred, reducing the balance of funds reserved.

RUCO had not opposed that AAWC adjustment in that docket, but Staff did. The

Commission concluded at page 37 of Decision No. 71410 concerning this as follows:

... we do not believe that it is necessary or reasonable to adopt the Company's proposal for advance funding of a Reserve for Tank Maintenance at this time. Because the tank maintenance expense reserve account balance proposed by the Company is not based on known and measureable Company expenditures, we find the normalization of tank maintenance expenses proposed by Staff, which is based on a three year average of expenses for each district, to be the more reasonable alternative. Staff's normalization adjustment will therefore be adopted for each of the six water districts.

1 In summary, AAWC's proposed Reserve accrual was rejected, and the Commission  
2 adopted a normalized amount based on a three-year average, as had been proposed by  
3 Staff.

4  
5 **Q. Is the \$445,000 annual reserve addition proposed by the Company as the amount of**  
6 **test year Tank Maintenance Reserve Accrual Expense for Sun City Water based on**  
7 **known and measurable expenses?**

8 A. No. It is orders of magnitude higher than Sun City's actual test year expenditures. Per  
9 AAWC's Schedule C-2, page 29, line 15, the test year Tank Maintenance Expense for Sun  
10 City Water was \$29,062.

11 Additionally, RUCO 2-91(d) (dated 12/21/2009) asked AAWC to:

12 "Provide the Company's actual tank painting expense, by district, by year,  
13 for the ten-year period through 2009. Also indicate which specific tanks  
14 were painted in each year, and the cost of painting each tank."  
15

16 AAWC's response to RUCO 2-91(d) stated in full: "Please see the attachment labeled  
17 "RUCO 2-91d Tank Painting Expenditures.xls" for maintenance detail by district.

18 Invoices are also included in this file." The response only included information for the  
19 2008 test year, and not for the ten-year period through 2009 as had been requested.

20 RUCO has notified the Company about its deficient response; however, as of the time of  
21 this writing, the Company has not supplemented its initial response to RUCO 2-91(d) to  
22 provide the requested information.

23  
24 **Q. Please explain RUCO adjustment C-8.**

1 A. This adjustment is shown on Attachment RCS-6, Schedule C-8 and removes the \$445,000  
2 additional pro forma accrual that AAWC seeks for Sun City Water to fund a Tank  
3 Maintenance Reserve. The Company seeks to collect from ratepayers in advance for tank  
4 maintenance. This Company request should be rejected because the tank maintenance  
5 expense reserve account balance proposed by the Company is not based on known and  
6 measureable Company expenditures and it is not necessary or reasonable to adopt the  
7 Company's proposal for advance funding of a Reserve for Tank Maintenance at this time.  
8 As noted above, a similar AAWC proposal was opposed by Staff and rejected by the  
9 Commission in Decision No. 71410.

10 **2. Anthem Water Tank Maintenance Reserve Fund Accrual**

11 **Q. Should a Reserve Fund Accrual be authorized for Anthem Water at this time?**

12 A. In Mr. Broderick's rebuttal testimony at page 10, AAWC is now apparently also  
13 requesting that a tank painting and inspections deferral be approved for Anthem Water  
14 District. As noted above, such Reserve Fund Accruals require pre-payment by ratepayers  
15 of expenses before they are incurred by the utility, and have undesirable features  
16 associated with single-issue ratemaking. Additionally, AAWC has not demonstrated that a  
17 Tank Maintenance Reserve Fund Accrual is necessary, reasonable or appropriate for  
18 Anthem Water at this time. Consequently, I recommend that AAWC's rebuttal filing  
19 request for authorization for a Reserve Fund Accrual for Anthem Water be rejected.  
20

21 ***Affiliated Management Fees (All Districts)***

22 **Q. Please briefly describe the Management Fees that AAWC incurs from affiliates.**

1 A. A considerable amount of AAWC's expenses come from affiliated company Management  
2 Fee charges. For the 2008 test year, AAWC recorded affiliated Management Fees charged  
3 to O&M expenses of approximately \$11.62 million, per the Company's response to  
4 RUCO 4-1. In addition, AAWC's original filing requested pro forma increases to this  
5 expense of approximately \$358,000.

6  
7 **Q. What pro forma adjustments did AAWC make to the affiliated Management Fees?**

8 A. AAWC made three pro forma adjustments to increase the net amount of affiliated  
9 Management Fee expense above the amount recorded in the 2008 test year for the five  
10 districts by approximately \$358,000 as summarized below:

**AAWC Affiliate Management Fee Pro Formas**

AAWC Adj.	Description	Increase (Decrease)
MHK-3	Increase labor by 4% and benefits by 22%	\$ 364,586
MHK-4	Increase "Other" by 4%	\$ 81,530
MHK-5	Remove costs for corporate divestiture and non- recurring projects	\$ (88,188)
	Net Increase to Test Year Recorded Amount of Affiliate Management Fees	\$ 357,928

11  
12  
13 **Q. How have you adjusted AAWC's request for Affiliate Management Fees?**

14 A. I have adjusted the affiliated Management Fees requested by AAWC in the following  
15 manner:

- 16 • In my direct testimony I had allowed the 4 percent affiliated Service Company pay  
17 increase that AAWC represents occurred in March 2009. Based on Commissioner  
18 interest in the recent open meeting in a UNS Gas rate case concerning utility post-  
19 test year pay increases, and RUCO's own re-evaluation of this issue in view of the

1 economic circumstances, RUCO has requested that I remove from test year  
2 operating expenses the affiliated Service Company's post test year pay increase. I  
3 have removed this affiliate post test year pay increase in Adjustment C-9A.

- 4 • I accepted AAWC's adjustment to remove one-time charges associated with  
5 corporate divestiture and non-recurring projects.
- 6 • I reversed AAWC's proposed 4 percent pro forma increase for "Other Expense"  
7 (Adjustment C-9).
- 8 • I removed AAWC's proposed 22 percent increase in employee benefits, which  
9 includes a one-year 72.92 percent increase for pensions and a 26.34 percent  
10 increase for OPEB, and assumed 4 percent increases for a number of other items,  
11 including state and federal unemployment taxes (Adjustment C-10).
- 12 • I removed all incentive compensation expense included in the Management Fees  
13 (Adjustment C-11).
- 14 • I adjusted the 2008 recorded pension amount to a normalized amount based on a  
15 two-year average of 2007-2008 (Adjustment C-12).
- 16 • I adjusted the 2008 recorded OPEB amount to a normalized amount based on a  
17 two-year average of 2007-2008 (Adjustment C-13).
- 18 • I removed the cost for the AWWSC "Business Development" function  
19 (Adjustment C-14).

20 Each of these adjustments is discussed in a subsequent section of my surrebuttal  
21 testimony.  
22

1 **Q. Has AAWC agreed to some of your recommended adjustments to affiliated**  
2 **Management Fee expense?**

3 A. AAWC witness Kiger's rebuttal testimony at page 11 indicates AAWC has accepted these  
4 adjustments to the affiliated Management Fee expenses:

- 5 ○ C-7, Dues and Donations
- 6 ○ C-9, Remove 4% Increase to "Other Expense"
- 7 ○ C-14, Remove Business Development Expense

8 AAWC is disputing these items:

- 9 ○ C-10, Remove 22.22% Post Test Year Increase for Affiliate Employee Benefits
- 10 ○ C-11, Affiliate Management Fees – Remove Affiliate Incentive Compensation
- 11 Expense
- 12 ○ C-12, Affiliate Management Fees – Normalize Affiliate Pension Expense
- 13 ○ C-13, Affiliate Management Fees – Normalize Affiliate OPEB Expense

14 I will address these affiliated Management Fee expense adjustments, focusing on the items  
15 that AAWC is disputing. In doing so, please note that I have already addressed, to some  
16 extent, affiliate incentive compensation, pension and OPEB issues above, in my  
17 surrebuttal testimony when discussing these issues in the context of AAWC direct  
18 expenses. Some of the same concerns that apply to AAWC's direct expenses for these  
19 items also apply to the affiliated Management Fee charges for such items.

20  
21 **C-9 Affiliate Management Fees – Remove 4% Increase to "Other Expense"**

22 **Q. Please summarize your recommended adjustment.**



A. This adjustment removes AAWC's requested post-test year increase to Affiliate Management Fees of 4 percent for "Other Expense". Expense for the five districts is reduced by \$81,530 as shown on Schedule C-9 and summarized on the table below.

Summary of Adjustments to Management Fees - Other Expenses

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (15,954)	\$ (20,793)	\$ (21,050)	\$ (12,855)	\$ (10,878)	\$ (81,530)

AAWC's rebuttal agreed with this adjustment.

**C-9A Affiliate Management Fees – Remove 4% March 2009 Pay Increase**

**Q. Please summarize your recommended adjustment.**

A. This adjustment is shown on Attachment RCS-6 and RCS-7, Schedule C.1, as Adjustment C-9A. It reduces AAWC's requested expense to remove a 4 percent pay increase that AAWC represents occurred in March 2009 for affiliated Service Company employees. As described above, in the past RUCO has agreed to post test year wage increases that took place shortly after the end of the test year. RUCO also believes generally that the consistent application of regulation is good public policy and provides for a stable regulatory environment. However, given the economic situation, Arizona's high unemployment and foreclosure rate, the size of the increases being requested in the instant case by AAWC, and the interest shown by Commissioners in the recent open meeting concerning a rate increase by UNS Gas, (Docket No. G-04024A-08-0571) RUCO has reconsidered its position on this issue and has requested that I remove this post test year wage increase. This adjustment reduces AAWC's requested operating expenses for the six districts by \$89,678. The amounts for each district are shown below:

Summary of Adjustments to Management Fees - Remove 4% Post-Test Year Wage Increase

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (17,548)	\$ (22,871)	\$ (23,154)	\$ (14,140)	\$ (11,965)	\$ (89,678)

**C-10 Affiliate Management Fees – Remove 22.22% Post Test Year Increase for Affiliate Employee Benefits**

**Q. Are you making any changes to Adjustment C-10 as a result of AAWC's rebuttal?**

**A. No.** AAWC witness Kiger's rebuttal at page 12, lines 8-10, acknowledges that a 22.2 percent increase is "larger-than-typical" but he nevertheless claims it should be borne by ratepayers because it "was driven by the increase in the known and measurable pension funding obligation under ERISA requirements for 2009." He thus attempts to impose a "larger-than-typical" increase on the test year based on 2009 ERISA funding amounts. As I have explained above, in conjunction with Adjustment C-5, 2009 was a highly abnormal year for pension expense. Moreover, the parent company, AWWC, has put shareholders on notice via statements in its SEC Form 10-K, that:

**The disruption in the capital markets and its actual or perceived effects on particular businesses and the greater economy also adversely affects the value of the investments held within the Company's employee benefit plan trusts. Significant declines in the value of the investments held within the Company's employee benefit plant trusts may require the Company to increase contributions to those trusts in order to meet future funding requirements if the actual asset returns do not recover these declines in value in the foreseeable future. These trends may also adversely impact the Company's results of operations, net cash flows and financial positions, including our shareholder's equity.**  
(Emphasis supplied.)

1           AWWC has already put its shareholders on notice, per page 28 of AWWC's SEC  
2           Form 10-K, that **"increases in pension and other postretirement costs as a result of**  
3           **reduced plan assets may not be fully recoverable from our customers."**

4           I disagree with Mr. Kiger's position stated at page 12, lines 16-18 that "Arizona-  
5           American must recover all of its known and measureable pension expense, especially  
6           pension expense related to the Service Company, in order for it to recover its cost of  
7           service." I disagree with this AAWC position because the function of ratemaking is not to  
8           guarantee that a utility can collect from ratepayers all of its expenses, including expenses  
9           that are unusually high during periods outside of a test year because of unprecedented  
10          market conditions. Rather, a reasonable and normal amount of expenses should be  
11          allowed. AAWC's 2009 pension expense, including the Service Company portion that is  
12          charged to AAWC through the affiliated Management Fee, is abnormally high in  
13          comparison with historical levels of such expense, and the reason it is abnormally high is  
14          due to unusual and perhaps unprecedented investment market conditions that were  
15          experienced. Such market conditions have alleviated somewhat, as evidenced by the  
16          negative pension plan asset return achieved by AWWC in 2008 versus the relatively  
17          robust return achieved in 2009. Basing rates on a 2009 amount of pension expense for  
18          AAWC directly or for the affiliated Service Company, as AWWC has requested, should  
19          be rejected.

20          Removing AAWC's requested 22.2 percent post test year increase for Service  
21          Company benefit costs is thus a necessary adjustment, and should be adopted. This  
22          adjustment removes AAWC's requested post-test year increase to Affiliate Management  
23          Fees for a 22.22 percent increase in affiliate employee benefit costs. The Company has

requested percentage increases in affiliate employee benefits expense and payroll taxes as follows:

Post Test Year Percentage Increases In Affiliate Employee Benefits Requested by AAWC	
Account	Percent Increase Over 2008
504100 Group Insurance	0.00%
505100 PBOP	26.34%
506100 Pension	72.92%
507100 401k	4.00%
508100 EIP	4.00%
508101 DCP	4.00%
508200 ESPP Oper AG	4.00%
685320 FUTA	4.00%
685325 FICA	4.00%
685350 SUTA	4.00%
Affiliate Employee Benefits Weighted Average Increase	22.22%

The affiliate expenses for pensions and OPEB (PBOP) are being addressed below, by adjusting the 2008 test year recorded amount to a normalized amount, based on a three-year average of 2006-2008. AAWC has failed to substantiate that the other expense, such as affiliate federal and state unemployment taxes and other benefits should be increased beyond the test year recorded level. Expense for the five districts is reduced by \$274,909 as shown on Schedule C-10, summarized on the table below.

Summary of Adjustments to Management Fees - Affiliate Employee Benefits

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (53,795)	\$ (70,111)	\$ (70,978)	\$ (43,347)	\$ (36,678)	\$ (274,909)

**C-11 Affiliate Management Fees – Remove Affiliate Incentive Compensation Expense**

**Q. Have you revised Adjustment C-11 as a result of AAWC's rebuttal testimony?**

A. No. This adjustment removes all identifiable incentive compensation expense included in the affiliate Management Fees for the 2008 test year. Expense for the five districts is reduced by \$256,853 as shown on Schedule C-11 and summarized on the schedule below.

Summary of Adjustments to Management Fees - Affiliate Incentive Compensation

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (50,261)	\$ (65,506)	\$ (66,317)	\$ (40,500)	\$ (34,269)	\$ (256,853)

**Q. Why should 100 percent of the affiliate incentive compensation expense be removed in the current AAWC rate case, when only 30 percent was removed in two recent AAWC rate cases?**

A. A 30 percent disallowance for incentive compensation was used for AAWC employees and for allocated Service Company incentive compensation in recent prior AAWC rate cases, including Decision Nos. 71410 and 68858. This was apparently done because the parties to those prior cases, which included AAWC, Staff and RUCO, did not attempt to distinguish the source of the financial trigger leading to the payment of incentive compensation, and apparently made no distinction between incentive compensation for AAWC's own employees, and the incentive compensation expense charged to AAWC for affiliated Service Company employees as part of the Management Fee.

The AIP plan indicates that, in 2008, more than 85% of the operating income target for the entire Company (meaning the parent, AWWC) had to be achieved before incentive compensation was awarded based on the corporate financial component of the

1 Plan, although such an award could be made on the Divisional/Regional and State  
2 financial components if operating income exceeded 85% of the target. In addition, more  
3 than 75% of the Corporate operating income target had to be achieved in order for any  
4 payments to be made on any components of the Plan for the entire Company.

5 Consequently, I believe it is reasonable and appropriate to exclude 100 percent of the  
6 incentive compensation expense that is charged to AAWC for affiliated Service Company  
7 employees as part of the American Water Works Management Fee charges. American  
8 Water Works' corporate financial income is only moderately influenced by AAWC  
9 operating results and is heavily influenced by non-Arizona jurisdictional operations, and is  
10 also impacted by American Water Works' non-regulated operations.

11 Additionally, as described above, in conjunction with my discussion of Adjustment  
12 C-3, Karla O. Teasley, the President of Illinois-American Water Company has  
13 acknowledged in public testimony that her water utility (which is an affiliate of AAWC)  
14 has been denied recovery of incentive compensation expense by the regulatory authority  
15 in that jurisdiction due to the presence of a parent company financial trigger.<sup>26</sup>  
16 Additionally, in a recent decision, the West Virginia Commission (while allowing utility  
17 direct incentive compensation expense) disallowed affiliate incentive compensation  
18 expense (as well as merit increases for utility employees) because such expenses were  
19 determined to be unreasonable during periods of economic hardship and high  
20 unemployment, and consequently were deemed to not meet a prudence test given the  
21 recent financial conditions and economic turmoil.<sup>27</sup>

<sup>26</sup> See excerpt from her testimony in ICC Docket 09-0319, included in Attachment RCS-8.

<sup>27</sup> Excerpts from an Order dated November 30, 2009, of the West Virginia Commission in a rate case decision involving Dominion Hope Gas are also included in Attachment RCS-8.

1           A disallowance of 100 percent of the incentive compensation for the affiliated  
2           Service Company employees who charge AAWC via the Management Fee is appropriate  
3           because the award to Service Company employees is dependent upon AWWC corporate  
4           operating income and corporate financial targets. It is inappropriate to charge AAWC  
5           ratepayers for affiliate incentive compensation that is premised on a parent company  
6           financial trigger. The AWWC corporate operating income and corporate financial results  
7           are influenced by operating income of non-jurisdictional and non-regulated operations of  
8           American Water Works. Arizona ratepayers should not have to pay for incentive  
9           compensation that is tied to American Water Works corporate or non-jurisdictional and  
10          non-regulated income or on non-Arizona jurisdictional operations or non-regulated  
11          operations-based financial achievements.

12  
13   **C-12   Affiliate Management Fees – Normalize Affiliate Pension Expense**

14   **Q.    Are you modifying Adjustment C-12 as a result of AAWC's rebuttal?**

15   **A.**   No. This adjustment normalizes the amount of affiliate pension expense that was included  
16          in the Management Fee charges to AAWC for the 2008 test year. The affiliate employees  
17          participate in the same AWWC pension plan (subject to eligibility restrictions) as do  
18          AAWC employees. Similar to the adjustment for the pension expense for AAWC,  
19          discussed above in conjunction with Adjustment C-5, I have provided for a normalized  
20          expense based on a two-year average of 2007-2008. Expense for the five districts is  
21          reduced by \$4,257 as shown on Schedule C-12, summarized on the table below.

Summary of Adjustments to Management Fees - Affiliate Pension Expense

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (833)	\$ (1,086)	\$ (1,099)	\$ (671)	\$ (568)	\$ (4,257)

**Q. Do you have any other comments on pension expense?**

**A.** Yes. This adjustment is not very large. The most important issues concerning pension expense for AAWC direct employees and for Service Company allocated costs for pension expense involve the removal of the abnormally high 2009 amounts that AAWC has requested, which are addressed, along with other issues relating to pension expense in my surrebuttal testimony above, in conjunction with Adjustments C-5 and C-10.

**C-13 Affiliate Management Fees – Normalize Affiliate OPEB Expense**

**Q. Are you modifying Adjustment C-13 as a result of AAWC's rebuttal?**

**A.** No. This adjustment normalizes the amount of OPEB expense that was included in the affiliate Management Fee charges to AAWC for the 2008 test year. The affiliate employees participate in the same AWWC OPEB plan (subject to eligibility restrictions) as do AAWC employees. Similar to the adjustment for the pension expense for AAWC, discussed above in conjunction with Adjustment C-6, I have provided for a normalized expense based on a two-year average of 2006-2008. Expense for the five districts is reduced by \$7,206 as shown on Schedule C-13 and summarized on the table below.

Summary of Adjustments to Management Fees - Affiliate OPEB Expense

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (1,410)	\$ (1,838)	\$ (1,860)	\$ (1,136)	\$ (961)	\$ (7,206)



1  
2 **Q. What other comments do you have about this adjustment?**

3 A. This adjustment is not very large. As noted above, the Company's attempt to use a 2009  
4 amount for OPEBs has a much smaller impact than its request to use an abnormally high  
5 2009 amount for pension expense. I address pension expense for AAWC direct  
6 employees and for Service Company allocated costs for pension expense involving the  
7 removal of the abnormally high 2009 amounts that AAWC has requested along with other  
8 issues related to pension expense in my surrebuttal testimony above, in conjunction with  
9 Adjustments C-5 and C-10.  
10

11 **C-14 Affiliate Management Fees – Remove Affiliate “Business Development” Costs**

12 **Q. Please explain Adjustment C-14.**

13 A. This adjustment removes all identifiable affiliate “Business Development” costs included  
14 in the affiliate Management Fees for the 2008 test year. Expense for the five districts is  
15 reduced by \$48,232 as shown on Schedule C-14 and as summarized in the table below.

Summary of Adjustments to Management Fees - Affiliate Business Development Costs

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (9,438)	\$ (12,301)	\$ (12,453)	\$ (7,605)	\$ (6,435)	\$ (48,232)

16  
17 These charges should be removed because they are unnecessary for the provision of safe,  
18 reliable and reasonably priced water and wastewater utility service in Arizona. Similar  
19 costs were removed by the California PUC in the most recent California American Water  
20 rate case.

21 AAWC has agreed in its rebuttal filing that these expenses should be removed.

**C-15 Interest Synchronization (All Districts)**

**Q. Have you updated Adjustment C-15?**

A. Yes. The interest synchronization adjustment applies the weighted cost of debt to the calculation of test year income tax expense. After adjustments, my proposed rate base differs from that of the Company. Additionally, the weighted cost of debt recommended by RUCO witness Rigsby differs from that requested by AAWC. This results in an adjustment to the amount of synchronized interest included in the tax calculation. The calculation of the interest synchronization adjustment is shown on Attachments RCS-6 (for water) and RCS-7 (for wastewater), Schedule C-15. This adjustment decreases income tax expense and increases the Company's achieved operating income by a similar amount, as summarized in the below table.

Summary of Adjustments to Income Tax Expense for Interest Synchronization

District	Anthem Water	Sun City Water	Anthem/ Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater	Total
Adjustment	\$ (9,934)	\$ 17,357	\$ 19,177	\$ (1,096)	\$ (6,977)	\$ 18,527

**C-16 Depreciation Expense (Sun City Water)**

**Q. Have you revised RUCO Adjustment C-16 as a result of AAWC's rebuttal?**

A. No. As shown on Attachment B-6, Schedule C-16, AAWC's proposed depreciation expense for Sun City Water is reduced by \$36,961 based on applying the applicable depreciation rates to the plant adjustment. The related adjustment to plant was discussed above in conjunction with my rate base adjustment B-1.

**C-17 Depreciation Expense (Agua Fria Wastewater)**

**Q. Have you revised RUCO Adjustment C-17 as a result of AAWC's rebuttal?**

A. No. This adjustment is shown on Attachment RCS-7, Schedule C-7 and reduces depreciation expense for Anthem/Agua Fria Wastewater by \$2,853 relating to the removal of two 75-horsepower pumps that were retired from plant in service. The retirement of those pumps was covered in my rate base shown on Attachment RCS-7, Schedule B-7, discussed above. AAWC indicated in its rebuttal filing that it agreed with the removal of such pumps.

**C-18 Depreciation Expense (Anthem Water)**

**Q. Please explain Adjustment C-18.**

A. This adjustment reflects the impact in Depreciation Expense related to a reclassification of \$22,289 from Account 304300 to Account 320100, as described above, under "Other Rate Base Adjustments". Depreciation Expense for Anthem Water is increased by \$1,202 as shown on Attachment RCS-6, Schedule C-18.

**C-19 Depreciation Expense (Anthem/Agua Fria Wastewater)**

**Q. Please explain Adjustment C-19.**

A. This adjustment reflects the impact on Depreciation Expense related to a reclassification of \$487,000 from Account 354400, Structures and Improvements, to Account 355500, Power Generation Equipment, as described above, under "Other Rate Base Adjustments". Depreciation Expense for Anthem/Agua Fria Wastewater is increased by \$13,392 as shown on Attachment RCS-7, Schedule C-19.

**Other Expense Adjustments**

**Q. Have you evaluated all of the expense adjustments addressed in AAWC's rebuttal?**

A. No. Failure to address an adjustment in my surrebuttal testimony that was discussed in AAWC's rebuttal should not be interpreted as either an endorsement in favor of, or a position against, making such adjustments.

**V. AAWC'S REBUTTAL FILING REQUEST FOR A MAJOR NEW ACCOUNTING DEFERRAL**

**Q. Has AAWC made a request in its rebuttal filing for a major new accounting deferral?**

A. Yes. AAWC witness Kiger's rebuttal testimony has presented a new Company request for a major new accounting deferral. Specifically, AAWC seeks authority to defer replacement costs paid to the City of Glendale in association with the 99<sup>th</sup> Avenue Interceptor, pursuant to a City of Glendale Sewage Transportation Agreement ("Glendale Agreement"). Mr. Kiger's rebuttal testimony attaches the Glendale Agreement to his rebuttal testimony in his Rebuttal Exhibit MHK-1R, and has attached a replacement cost invoice from the City of Glendale in his Rebuttal Exhibit MHK-2R. That invoice is dated November 6, 2009 and bills AAWC for \$917,906 for 99<sup>th</sup> Avenue Interceptor Repair Costs. Mr. Kiger's Rebuttal Exhibit MHK-3R presents a 99<sup>th</sup> Avenue Interceptor Proposed Budget for fiscal years ending 9/30/2010 through 9/30/2017. That document indicates a "Revision Date" of 12/15/2009. At page 3 of Mr. Kiger's rebuttal testimony, AAWC "requests that the Commission authorize an accounting order in the decision in

1           this case to defer these costs, as well as future similar costs, for consideration of rate  
2           recovery in a future rate case.”  
3

4       **Q.    Should this AAWC rebuttal filing request for a major new accounting deferral be**  
5       **granted in the current AAWC rate case?**

6       A.    No. The Glendale invoice that bills AAWC for \$917,906 is dated November 6, 2009.  
7           Presumably AAWC was aware of this since early November 2009. For AAWC to wait  
8           several months, until its rebuttal filing on March 22, 2010, to raise this issue puts the other  
9           interested parties at a disadvantage. AAWC’s receipt of the Glendale invoice occurred  
10          well after the end of the test year, and may be in dispute between AAWC and Glendale.  
11          Thus, it is not apparent why this issue needs to be decided in the current AAWC rate case.  
12          Perhaps it could be more appropriately addressed in a separately filed request for an  
13          accounting deferral, similar to the Company’s May 15, 2009 request for an accounting  
14          deferral filed in Docket No. 09-0241 for pensions. As a separate filing, this request by  
15          AAWC can receive the attention and scrutiny it deserves. As another rate case issue,  
16          presented for the first time in AAWC’s rebuttal, it may not receive adequate scrutiny, and  
17          a full record including explanations concerning the apparently retroactive billing from  
18          Glendale may be lacking.  
19

20       **Q.    Why do you say there are concerns about the apparently retroactive billing?**

21       A.    There are concerns about this large and apparently at least partially retroactive billing. At  
22          page 3, line 19 of his rebuttal, Mr. Kiger states that the \$917,906 relates to replacements

1           that occurred from December 2005 to April 2009. This raises issues about retroactive cost  
2           recovery.

3  
4       **Q.    What other concerns are presented by this AAWC request?**

5       A.    Singling out such a billing for special accounting or ratemaking treatment also raises  
6           concerns about single-issue ratemaking.

7                   Additionally, at page 3, lines 9-13, Mr. Kiger states that AAWC has not yet paid  
8           the invoice, and the amount the Company ultimately pays may differ from the invoiced  
9           amount as discussions continue between AAWC and the City of Glendale. Given these  
10          circumstances, the invoiced amount does not appear to be a known and measurable  
11          expense, especially in the context of the 2008 test year being used in the current AAWC  
12          rate case.

13  
14       **Q.    What do you recommend?**

15       A.    Because of the timing of its request – presented for the first time in AAWC's rebuttal –  
16           and because of such other concerns briefly described above, this request by AAWC for a  
17           major new accounting deferral should be rejected in the current AAWC rate case.

18  
19       **Q.    Does this conclude your testimony?**

20       A.    Yes, it does.

**Arizona American Water Company**  
**Docket No. W-01303A-09-0343**  
**Attachment RCS-6**  
**Accompanying the Surrebuttal Testimony of Ralph Smith**  
**RUCO Accounting Schedules - Water Districts**

Number	Description	No. of Pages	Page No.	Revised/ New
<b>Revenue Requirement Summary Schedules - Total Water</b>				
A	Calculation of Revenue Deficiency (Sufficiency)	1	2	Revised
A-1	Gross Revenue Conversion Factor	1	3	Revised
B	Adjusted Rate Base	1	4	Revised
B.1	Summary of Rate Base Adjustments	1	5	Revised
C	Adjusted Net Operating Income	1	6	Revised
C.1	Summary of Net Operating Income Adjustments	4	7-10	Revised
D	Capital Structure and Cost Rates	1	11	
<b>Revenue Requirement Summary Schedules - Anthem Water</b>				
A (A)	Calculation of Revenue Deficiency (Sufficiency)	1	12	Revised
A-1(A)	Gross Revenue Conversion Factor	1	13	Revised
B(A)	Adjusted Rate Base	1	14	Revised
B.1(A)	Summary of Rate Base Adjustments	1	15	Revised
C(A)	Adjusted Net Operating Income	1	16	Revised
C.1(A)	Summary of Net Operating Income Adjustments	3	17-19	Revised
<b>Revenue Requirement Summary Schedules - Sun City Water</b>				
A (SC)	Calculation of Revenue Deficiency (Sufficiency)	1	20	Revised
A-1(SC)	Gross Revenue Conversion Factor	1	21	Revised
B (SC)	Adjusted Rate Base	1	22	Revised
B.1 (SC)	Summary of Rate Base Adjustments	1	23	Revised
C (SC)	Adjusted Net Operating Income	1	24	Revised
C.1 (SC)	Summary of Net Operating Income Adjustments	3	25-27	Revised
<b>Rate Base Adjustments</b>				
B-1	Post-Test Year Additions to Plant - Well 5.1 - Sun City Water	1	28	
B-3	Contributions In Aid of Construction	1	29	
B-4	Cash Working Capital	3	30-32	Revised
B-5	Youngtown Plant - Sun City Water	1	33	New
B-9	Accumulated Deferred Income Taxes	1	34	New
<b>Net Operating Income Adjustments</b>				
C-1	Customer Annualization Correction - Anthem Water	1	35	Revised
C-2	Rate Case Expense	1	36	
C-3	Achievement Incentive Pay	1	37	
C-4	Stock-Based Compensation	1	38	Revised
C-5	Pension Expense	1	39	
C-5.1	Calculations for pension expense adjustment	2	40-41	
C-6	OPEB Expense	1	42	
C-7	Dues, Donations & Miscellaneous Expenses	1	43	
C-8	Tank Maintenance Expense - Sun City Water	1	44	
C-9	Management Fees - Other Expenses	1	45	
C-10	Management Fees - Remove AAWC's Requested Post Test Year Increase in Affiliate Employee Benefits	1	46	
C-11	Management Fees - Remove Affiliate Incentive Compensation Expense	1	47	
C-12	Management Fees - Normalize Affiliate Pension Expense	1	48	
C-13	Management Fees - Normalize Affiliate OPEB Expense	1	49	
C-14	Management Fees - Remove Business Development Expense	1	50	
C-15	Interest Synchronization	1	51	Revised
C-16	Depreciation Expense - Well 5.1 - Sun City Water	1	52	
C-18	Depreciation Expense - Anthem Water Reclassified Accounts	1	53	New
Total Pages (including Contents page)		53		

Arizona American Water Company - Total of Water Districts  
Calculation of Revenue Deficiency (Sufficiency)

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule A  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B	\$ 85,616,088	\$ 83,474,455	\$ (2,141,633)
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 7,303,090	\$ 5,654,560	\$ (1,648,530)
4	Adjusted net operating income	C	\$ 1,375,533	\$ 2,043,394	\$ 667,861
5	Net operating income deficiency		\$ 5,927,557	\$ 3,611,166	\$ (2,316,391)
6	Gross revenue conversion factor	A-1	1.6561	1.6561	
7	Revenue deficiency (Sufficiency)		\$ 9,816,374	\$ 5,980,307	\$ (3,836,067)

Percentage Increase Over Current Rates  
Revenue from Sales to Retail Customers  
Percentage Increase

Sch C, L.1 \$ 16,335,827 \$ 16,345,285  
L.7 / L.8 60.09% 36.59%

Notes and Source

Col.A: AAWC Filing, Schedule A-1 (Anthem and Sun City)

Calculation of RUCO recommended percentage increase to AAWC's base rates

AAWC's adjusted water revenues per Schedule C	RUCO Proposed
RUCO recommended rate increase (line 7 above)	\$ 16,345,285
Total revenues after reflecting RUCO recommended increase	\$ 5,980,307
Percentage change in revenues	\$ 22,325,592
	36.59%

Calculation of AAWC's proposed percentage increase to base rates

AAWC's adjusted water revenues per Schedule C	AAWC Proposed
AAWC proposed rate increase (line 7 above)	\$ 16,335,827
Total revenues after reflecting AAWC proposed increase	\$ 9,816,374
Percentage change in revenues	\$ 26,152,201
	60.09%



Arizona American Water Company  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule A-1  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.71%	0.71%
3	Bad Debt Expense	0.31%	0.31%
4	Taxable Income as a Percent	98.98%	98.98%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.35%	67.35%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.38%	60.38%
9	<b>Gross Revenue Conversion Factor</b>	<b>1.6561</b>	<b>1.6561</b>

Notes and Source

Col.A: AAWC Filing, Schedule C-3

Combined state and federal income tax rate 38.60% 38.60%

**Components of Revenue Requirement Increase**

	Amount	Percent
11 Net Income	\$ 3,611,172	60.38%
12 Federal Income Taxes	\$ 1,891,624	31.63%
13 State Income Taxes	\$ 416,708	6.97%
14 Property Taxes	\$ 42,246	0.71%
15 Uncollectibles	\$ 18,557	0.31%
16 Total Revenue Increase	\$ 5,980,307	100.00%
17 Total Revenue Increase (From Schedule A)	\$ 5,980,307	

Arizona American Water Company - Total of Water Districts  
Adjusted Rate Base

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 149,301,020	\$ (1,272,682)	\$ 148,028,338
2	Phoenix Interconnection	\$ 5,000,000		\$ 5,000,000
3	Amortization of Phoenix Interconnection	\$ (116,667)		\$ (116,667)
4	Accumulated Depreciation	\$ (31,762,996)	\$ (441,956)	\$ (32,204,952)
5	<b>Net Utility Plant in Service</b>	<b>\$ 122,421,357</b>	<b>\$ (1,714,638)</b>	<b>\$ 120,706,719</b>
<b>Less:</b>				
6	Advances in Aid of Construction	\$ (24,418,393)	\$ -	\$ (24,418,393)
7	Contributions in Aid of Construction (net of amortization)	\$ (15,572,984)	\$ (69,262)	\$ (15,642,246)
8	Imputed Regulatory Advances	\$ -	\$ -	\$ -
9	Imputed Regulatory Contributions	\$ (669,222)	\$ -	\$ (669,222)
10	Customer Meter Deposits	\$ (4,370)	\$ -	\$ (4,370)
11	Deferred Income Taxes and Credits	\$ 2,624,884	\$ (67,731)	\$ 2,557,153
12	Investment Tax Credits and Deferred Credits	\$ -	\$ -	\$ -
13	<b>Total Reductions</b>	<b>\$ (38,040,085)</b>	<b>\$ (136,993)</b>	<b>\$ (38,177,078)</b>
<b>Plus:</b>				
14	Unamortized Finance Charges	\$ -	\$ -	\$ -
15	Deferred Tax Assets	\$ -	\$ -	\$ -
16	Deferred Debits	\$ 489,620	\$ -	\$ 489,620
17	Allowance for Working Capital	\$ 745,195	\$ (290,000)	\$ 455,195
18	Utility Plant Acquisition Adjustment	\$ -	\$ -	\$ -
19	<b>Total Additions</b>	<b>\$ 1,234,814</b>	<b>\$ (290,000)</b>	<b>\$ 944,814</b>
20	<b>Total Rate Base</b>	<b>\$ 85,616,088</b>	<b>\$ (2,141,631)</b>	<b>\$ 83,474,455</b>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1

Arizona American Water Company - Total of Water Districts  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B.1  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments	Post-Test Year Plant - Well 5.1 B-1	Contributions in Aid of Construction B-3		Cash Working Capital B-4 Revised	Youngstown Plant B-5		Accumulated Deferred Income Taxes B-9	
							New		New	
1	Gross Utility Plant in Service	\$ (1,272,682)	\$ (1,123,185)					\$ (149,497)		
2	Accumulated Depreciation	\$ (441,956)	\$ (463,954)					\$ 22,008		
3	Net Utility Plant in Service	\$ (1,714,638)	\$ (1,587,149)	\$ -	\$ -	\$ -		\$ (127,489)	\$ -	
<b>Less:</b>										
4	Advances in Aid of Construction	\$ -								
5	Contributions in Aid of Construction (net of amortization)	\$ (69,262)		\$ (69,262)						
6	Imputed Regulatory Advances	\$ -								
7	Imputed Regulatory Contributions	\$ -								
8	Deferred Income Taxes and Credits	\$ (67,731)							\$ (67,731)	
9	Investment Tax Credits and Deferred Credits	\$ -								
10	Total Reductions	\$ (136,993)	\$ -	\$ (69,262)	\$ -	\$ -		\$ -	\$ (67,731)	
<b>Plus:</b>										
11	Unamortized Finance Charges	\$ -								
12	Deferred Tax Assets	\$ -								
13	Deferred Debits	\$ -								
14	Allowance for Working Capital	\$ (290,000)			\$ (290,000)					
15	Utility Plant Acquisition Adjustment	\$ -								
16	Total Additions	\$ (290,000)	\$ -	\$ -	\$ (290,000)	\$ (290,000)		\$ -	\$ -	
17	Total Rate Base	\$ (2,141,631)	\$ (1,587,149)	\$ (69,262)	\$ (290,000)	\$ (290,000)		\$ (127,489)	\$ (67,731)	

Notes and Source

See referenced exhibit for each adjustment

Arizona American Water Company - Total of Water Districts  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule C  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Water Revenues	\$ 16,335,827	\$ 9,458	\$ 16,345,285
2	Other Revenues	\$ 430,548	\$ -	\$ 430,548
3	<b>Total Revenues</b>	<u>\$ 16,766,375</u>	<u>\$ 9,458</u>	<u>\$ 16,775,833</u>
<b>Operating Expenses</b>				
4	Labor	\$ 1,979,757	\$ (55,530)	\$ 1,924,227
5	Purchased Water	\$ 625,435	\$ -	\$ 625,435
6	Fuel & Power	\$ 2,982,219	\$ -	\$ 2,982,219
7	Chemicals	\$ 140,388	\$ -	\$ 140,388
8	Waste Disposal	\$ 1,933	\$ -	\$ 1,933
9	Management Fees	\$ 2,667,400	\$ (358,748)	\$ 2,308,652
10	Group Insurance	\$ 563,722	\$ (4,683)	\$ 559,039
11	Pensions	\$ 357,243	\$ (131,839)	\$ 225,404
12	Regulatory Expense	\$ 139,775	\$ (51,307)	\$ 88,468
13	Insurance Other Than Group	\$ 164,808	\$ -	\$ 164,808
14	Customer Accounting	\$ 418,449	\$ -	\$ 418,449
15	Rents	\$ 93,842	\$ -	\$ 93,842
16	General Office Expense	\$ 138,590	\$ -	\$ 138,590
17	Miscellaneous	\$ 529,384	\$ (7,487)	\$ 521,897
18	Maintenance Expense	\$ 793,404	\$ (445,000)	\$ 348,404
19	Depreciation & Amortization	\$ 3,965,599	\$ (35,759)	\$ 3,929,840
20	General Taxes - Property Taxes	\$ 449,027	\$ -	\$ 449,027
21	General Taxes - Other	\$ 129,794	\$ -	\$ 129,794
22	Income Taxes	\$ (749,929)	\$ 431,951	\$ (317,978)
23	<b>Total Operating Expenses</b>	<u>\$ 15,390,840</u>	<u>\$ (658,402)</u>	<u>\$ 14,732,438</u>
24	<b>Utility Operating Income</b>	<u>\$ 1,375,535</u>	<u>\$ 667,860</u>	<u>\$ 2,043,395</u>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -	\$ -	\$ -
26	Interest Expense	\$ (2,568,483)	\$ -	\$ (2,568,483)
27	Other Expense	\$ (32,427)	\$ -	\$ (32,427)
28	Gain/Loss Sale of Fixed Assets	\$ (7)	\$ -	\$ (7)
29	<b>Total Other Additions/Deductions From Income</b>	<u>\$ (2,600,917)</u>	<u>\$ -</u>	<u>\$ (2,600,917)</u>
30	<b>Net Profit (Loss)</b>	<u>\$ (1,225,382)</u>	<u>\$ 667,860</u>	<u>\$ (557,522)</u>
31	Rate Base	<u>\$ 85,616,088</u>	<u>\$ (170,851)</u>	<u>\$ 85,445,237</u>
32	Earned Rate of Return	<u>1.61%</u>		<u>2.39%</u>

Notes and Source

Col.A: AAWC Filing, Schedule C-1  
Col.B: Schedule C.1  
Col.C: Col.A + Col.B

Attachment RCS-6  
Docket No. W-01303A-09-0343  
Page 7 of 53

## Notes and Source

38.60%

Arizona American Water Company - Total of Water Districts  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-6  
Schedule C.1  
Docket No. W-01303A-09-0343  
Page 2 of 4  
Revised

Attachment RCS-6  
Docket No. W-01303A-09-0343  
Page 8 of 53

Line No.	Description	OPEB Expense C-6	Dues, Donations & Misc. Expenses C-7	Tank Maintenance Expense C-8	Management Fees - Other Expenses C-9	Management Fees - 4% Post-Test Year Wage Increase C-9A New
1	Revenues					
2	Water Revenues					
3	Other Revenues					
3	Total Revenues	\$ -	\$ -	\$ -	\$ -	\$ -
4	Operating Expenses					
4	Labor					
5	Purchased Water					
6	Fuel & Power					
7	Chemicals					
8	Waste Disposal					
9	Management Fees				\$ (36,747)	\$ (40,419)
10	Group Insurance	\$ (4,683)				
11	Pensions					
12	Regulatory Expense					
13	Insurance Other Than Group					
14	Customer Accounting					
15	Rents					
16	General Office Expense					
17	Miscellaneous		\$ (7,487)	\$ (445,000)		
18	Maintenance Expense					
19	Depreciation & Amortization					
20	General Taxes - Property Taxes					
21	General Taxes - Other					
15	PRE-TAX OPERATING EXPENSES	\$ (4,683)	\$ (7,487)	\$ (445,000)	\$ (36,747)	\$ (40,419)
16	PRE-TAX OPERATING INCOME	\$ 4,683	\$ 7,487	\$ 445,000	\$ 36,747	\$ 40,419
17	Income Taxes	\$ 1,808	\$ 2,890	\$ 171,770	\$ 14,184	\$ 15,602
18	TOTAL OPERATING EXPENSES	\$ (2,875)	\$ (4,597)	\$ (273,230)	\$ (22,563)	\$ (24,817)
19	OPERATING INCOME	\$ 2,875	\$ 4,597	\$ 273,230	\$ 22,563	\$ 24,817

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C-3

Arizona American Water Company - Total of Water Districts  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-6  
Schedule C.1  
Docket No. W-01303A-09-0343  
Page 3 of 4  
Revised

Line No.	Description	Management				Management		Management		Management	
		Management Fees - Employee Benefits	Management Fees - Incentive Compensation	Management Fees - Normalize Affiliate Pension Expense	Management Fees - Normalize Affiliate OPEB Expense	Management Fees - Remove Business Development Expenses	C-10	C-11	C-12	C-13	C-14
1	Revenues										
2	Water Revenues										
3	Other Revenues										
	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
4	Operating Expenses										
5	Labor										
6	Purchased Water										
7	Fuel & Power										
8	Chemicals										
9	Waste Disposal										
10	Management Fees	\$ (123,905)	\$ (115,767)	\$ (1,919)	\$ (3,248)	\$ (21,739)					
11	Group Insurance										
12	Pensions										
13	Regulatory Expense										
14	Insurance Other Than Group										
15	Customer Accounting										
16	Rents										
17	General Office Expense										
18	Miscellaneous										
19	Maintenance Expense										
20	Depreciation & Amortization										
21	General Taxes - Property Taxes										
15	General Taxes - Other	\$ (123,905)	\$ (115,767)	\$ (1,919)	\$ (3,248)	\$ (21,739)					
16	PRE-TAX OPERATING EXPENSES	\$ 123,905	\$ 115,767	\$ 1,919	\$ 3,248	\$ 21,739					
17	PRE-TAX OPERATING INCOME	\$ 47,827	\$ 44,686	\$ 741	\$ 1,254	\$ 8,391					
18	Income Taxes	\$ (76,078)	\$ (71,081)	\$ (1,178)	\$ (1,994)	\$ (13,348)					
19	TOTAL OPERATING EXPENSES	\$ 76,078	\$ 71,081	\$ 1,178	\$ 1,994	\$ 13,348					
	OPERATING INCOME										

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C-3

Arizona American Water Company - Total of Water Districts  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-6  
Schedule C.1  
Docket No. W-01303A-09-0343  
Page 4 of 4  
Revised

Attachment RCS-6  
Docket No. W-01303A-09-0343  
Page 10 of 53

Line No.	Description	Interest Synchronization C-15 Revised	Depreciation Expense - Related to Post-Test Year Plant - Well 5.1 C-16	Depreciation Expense - Anthem Water Reclassified Accounts C-18 New
<b>Revenues</b>				
1	Water Revenues			
2	Other Revenues			
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -
<b>Operating Expenses</b>				
4	Labor			
5	Purchased Water			
6	Fuel & Power			
7	Chemicals			
8	Waste Disposal			
9	Management Fees			
10	Group Insurance			
11	Pensions			
12	Regulatory Expense			
13	Insurance Other Than Group			
14	Customer Accounting			
15	Rents			
16	General Office Expense			
17	Miscellaneous			
18	Maintenance Expense			
19	Depreciation & Amortization		\$ (36,961)	\$ 1,202
20	General Taxes - Property Taxes			
21	General Taxes - Other			
15	PRE-TAX OPERATING EXPENSES	\$ -	\$ (36,961)	\$ 1,202
16	PRE-TAX OPERATING INCOME	\$ -	\$ 36,961	\$ (1,202)
17	Income Taxes	\$ 7,423	\$ 14,267	\$ (464)
18	TOTAL OPERATING EXPENSES	\$ 7,423	\$ (22,694)	\$ 738
19	OPERATING INCOME	\$ (7,423)	\$ 22,694	\$ (738)

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C-3



Arizona American Water Company - Water Districts  
Capital Structure and Cost Rates

Attachment RCS-6  
Schedule D  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Amount (A)	Percent (B)	Cost Rate (C)	Weighted Cost (D)
<b>Per Company</b>					
1	Long-Term Debt	\$ 188,208,140	54.85%	5.47%	3.00%
2	Short-Term Debt				
3	Stockholder's Equity	\$ 154,949,595	45.15%	12.25%	5.53%
4	Total	<u>\$ 343,157,735</u>	<u>100.00%</u>		<u>8.53%</u>
<b>Per RUCO</b>					
5	Long-Term Debt	\$ 188,208,140	47.56%	5.47%	2.60%
6	Short-Term Debt	\$ 52,584,000	13.29%	3.41%	0.45%
7	Stockholder's Equity	\$ 154,949,595	39.15%	9.50%	3.72%
8	Total	<u>\$ 395,741,735</u>	<u>100.00%</u>		<u>6.77%</u>
9	Difference				-1.756%
10	Weighted Cost of Debt				<u><u>3.05%</u></u>

Notes and Source

Lines 1-4: AAWC Filing, Schedule D-1 (reflects end of projected test year capital structure)  
Lines 5-8: Per RUCO witness William Rigsby (reflects end of test year capital structure)

Arizona American Water Company - Anthem Water  
Calculation of Revenue Deficiency (Sufficiency)

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule A (A)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B (A)	\$ 57,430,025	\$ 57,259,174	\$ (170,851)
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 4,898,781	\$ 3,878,736	\$ (1,020,045)
4	Adjusted net operating income	C (A)	\$ 514,448	\$ 683,807	\$ 169,359
5	Net operating income deficiency		\$ 4,384,333	\$ 3,194,929	\$ (1,189,404)
6	Gross revenue conversion factor	A-1 (A)	1.6578	1.6578	
7	Revenue deficiency (Sufficiency)		\$ 7,268,177	\$ 5,296,426	\$ (1,971,751)
Percentage Increase Over Current Rates					
8	Revenue from Sales to Retail Customers	Sch C (A), L.1	\$ 7,210,624	\$ 7,220,082	
9	Percentage Increase	L.7 / L.8	100.80%	73.36%	

Notes and Source

Col.A: AAWC Filing, Schedule A-1

Calculation of RUCO recommended percentage increase to AAWC's base rates

	RUCO Proposed
AAWC's adjusted water revenues per Schedule C (A)	\$ 7,220,082
RUCO recommended rate increase (line 7 above)	\$ 5,296,426
Total revenues after reflecting RUCO recommended increase	\$ 12,516,508
Percentage change in revenues	73.36%

Calculation of AAWC's proposed percentage increase to base rates

	AAWC Proposed
AAWC's adjusted water revenues per Schedule C (A)	\$ 7,210,624
AAWC proposed rate increase (line 7 above)	\$ 7,268,177
Total revenues after reflecting AAWC proposed increase	\$ 14,478,801
Percentage change in revenues	100.80%

Arizona American Water Company - Anthem Water  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule A-1 (A)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.80%	0.80%
3	Bad Debt Expense	0.28%	0.28%
4	Taxable Income as a Percent	98.92%	98.92%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.29%	67.29%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.32%	60.32%
9	Gross Revenue Conversion Factor	1.6578	1.6578

Notes and Source

Col.A: AAWC Filing, Schedule C-3

Combined state and federal income tax rate	38.60%	38.60%
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Components of Revenue Requirement Increase

	Amount	Percent
11 Net Income	\$ 3,194,927	60.32%
12 Federal Income Taxes	\$ 1,675,306	31.63%
13 State Income Taxes	\$ 369,055	6.97%
14 Property Taxes	\$ 42,423	0.80%
15 Uncollectibles	\$ 14,715	0.28%
16 Total Revenue Increase	\$ 5,296,426	100.00%
17 Total Revenue Increase (From Schedule A (A))	\$ 5,296,426	

Arizona American Water Company - Anthem Water  
Adjusted Rate Base

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B (A)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 85,684,602	\$ -	\$ 85,684,602
2	Phoenix Interconnection	\$ 5,000,000	\$ -	\$ 5,000,000
3	Amortization of Phoenix Interconnection	\$ (116,667)	\$ -	\$ (116,667)
4	Accumulated Depreciation	\$ (12,789,099)	\$ -	\$ (12,789,099)
5	<b>Net Utility Plant in Service</b>	<u>\$ 77,778,836</u>	<u>\$ -</u>	<u>\$ 77,778,836</u>
<b>Less:</b>				
6	Advances in Aid of Construction	\$ (18,557,742)	\$ -	\$ (18,557,742)
7	Contributions in Aid of Construction (net of amortization)	\$ (2,393,271)	\$ (30,271)	\$ (2,423,542)
8	Imputed Regulatory Advances	\$ -	\$ -	\$ -
9	Imputed Regulatory Contributions	\$ (326,764)	\$ -	\$ (326,764)
10	Customer Meter Deposits	\$ (1,920)	\$ -	\$ (1,920)
11	Deferred Income Taxes and Credits	\$ 720,067	\$ (18,580)	\$ 701,487
12	Investment Tax Credits and Deferred Credits	\$ -	\$ -	\$ -
13	<b>Total Reductions</b>	<u>\$ (20,559,630)</u>	<u>\$ (48,851)</u>	<u>\$ (20,608,481)</u>
<b>Plus:</b>				
13	Unamortized Finance Charges	\$ -	\$ -	\$ -
14	Deferred Tax Assets	\$ -	\$ -	\$ -
15	Deferred Debits	\$ 51,714	\$ -	\$ 51,714
16	Allowance for Working Capital	\$ 159,104 *	\$ (122,000)	\$ 37,104
17	Utility Plant Acquisition Adjustment	\$ -	\$ -	\$ -
18	<b>Total Additions</b>	<u>\$ 210,818</u>	<u>\$ (122,000)</u>	<u>\$ 88,818</u>
19	<b>Total Rate Base</b>	<u>\$ 57,430,025</u>	<u>\$ (170,851)</u>	<u>\$ 57,259,174</u>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1

\* Per Revised Schedule B-5 (Company did not revise Schedule B-1 for Anthem Water)

Arizona American Water Company - Anthem Water  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B.1 (A)  
Docket No. W-1303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments	Contributions in Aid of Construction B-3	Cash Working Capital B-4 Revised	Accumulated Deferred Income Taxes B-9 New	
1	Gross Utility Plant in Service	\$ -				
2	Phoenix Interconnection	\$ -				
3	Amortization of Phoenix Interconnection	\$ -				
4	Accumulated Depreciation	\$ -				
5	<b>Net Utility Plant in Service</b>	\$ -	\$ -	\$ -		\$ -
<b>Less:</b>						
6	Advances in Aid of Construction	\$ -				
7	Contributions in Aid of Construction (net of amortization)	\$ (30,271)	\$ (30,271)			
8	Imputed Regulatory Advances	\$ -				
9	Imputed Regulatory Contributions	\$ -				
10	Customer Meter Deposits	\$ -				
11	Deferred Income Taxes and Credits	\$ (18,580)			\$ (18,580)	
12	Investment Tax Credits and Deferred Credits	\$ -				
13	<b>Total Reductions</b>	\$ (48,851)	\$ (30,271)	\$ -	\$ (18,580)	
<b>Plus:</b>						
13	Unamortized Finance Charges	\$ -				
14	Deferred Tax Assets	\$ -				
15	Deferred Debits	\$ -				
16	Allowance for Working Capital	\$ (122,000)		\$ (122,000)		
17	Utility Plant Acquisition Adjustment	\$ -				
18	<b>Total Additions</b>	\$ (122,000)	\$ -	\$ (122,000)	\$ -	
19	<b>Total Rate Base</b>	\$ (170,851)	\$ (30,271)	\$ (122,000)	\$ (18,580)	
		\$ (170,851)				

Notes and Source

See referenced exhibit for each adjustment

Arizona American Water Company - Anthem Water  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule C (A)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Water Revenues	\$ 7,210,624	\$ 9,458	\$ 7,220,082
2	Other Revenues	\$ 272,650	\$ -	\$ 272,650
3	<b>Total Revenues</b>	<u>\$ 7,483,274</u>	<u>\$ 9,458</u>	<u>\$ 7,492,732</u>
<b>Operating Expenses</b>				
4	Labor	\$ 754,087	\$ (24,152)	\$ 729,935
5	Purchased Water	\$ 625,435	\$ -	\$ 625,435
6	Fuel & Power	\$ 1,259,637	\$ -	\$ 1,259,637
7	Chemicals	\$ 103,351	\$ -	\$ 103,351
8	Waste Disposal	\$ 1,933	\$ -	\$ 1,933
9	Management Fees	\$ 1,158,078	\$ (155,753)	\$ 1,002,325
10	Group Insurance	\$ 209,326	\$ (2,033)	\$ 207,293
11	Pensions	\$ 105,808	\$ (39,203)	\$ 66,605
12	Regulatory Expense	\$ 64,489	\$ (27,003)	\$ 37,486
13	Insurance Other Than Group	\$ 71,553	\$ -	\$ 71,553
14	Customer Accounting	\$ 183,101	\$ -	\$ 183,101
15	Rents	\$ 33,826	\$ -	\$ 33,826
16	General Office Expense	\$ 60,044	\$ -	\$ 60,044
17	Miscellaneous	\$ 229,300	\$ (3,250)	\$ 226,050
18	Maintenance Expense	\$ 140,803	\$ -	\$ 140,803
19	Depreciation & Amortization	\$ 2,399,893	\$ 1,202	\$ 2,401,095
20	General Taxes - Property Taxes	\$ 292,953	\$ -	\$ 292,953
21	General Taxes - Other	\$ 34,882	\$ -	\$ 34,882
22	Income Taxes	\$ (759,675)	\$ 90,292	\$ (669,383)
23	<b>Total Operating Expenses</b>	<u>\$ 6,968,825</u>	<u>\$ (159,901)</u>	<u>\$ 6,808,924</u>
24	<b>Utility Operating Income</b>	<u>\$ 514,448</u>	<u>\$ 169,359</u>	<u>\$ 683,807</u>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -		\$ -
26	Interest Expense	\$ (1,722,901)		\$ (1,722,901)
27	Other Expense	\$ (14,079)		\$ (14,079)
28	Gain/Loss Sale of Fixed Assets	\$ (3)		\$ (3)
29	<b>Total Other Additions/Deductions From Income</b>	<u>\$ (1,736,983)</u>	<u>\$ -</u>	<u>\$ (1,736,983)</u>
30	<b>Net Profit (Loss)</b>	<u>\$ (1,222,535)</u>	<u>\$ 169,359</u>	<u>\$ (1,053,176)</u>
31	Rate Base	<u>\$ 57,430,025</u>	<u>\$ (170,851)</u>	<u>\$ 57,259,174</u>
32	Earned Rate of Return	<u>0.90%</u>		<u>1.19%</u>

Notes and Source

Col.A: AAWC Filing, Schedule C-1  
Col.B: Schedule C.1  
Col.C: Col.A + Col.B

Arizona American Water Company - Anthem Water  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	RUCO Adjustments	Customer Annualization Correction C-1 Revised	Rate Case Expense C-2	Achievement Incentive Pay C-3	Stock-Based Compensation C-4 Revised	Pension Expense C-5	OPEB Expense C-6
<b>Revenues</b>								
1	Water Revenues	\$ 9,458	\$ 9,458					
2	Other Revenues	\$ -						
3	<b>Total Revenues</b>	<b>\$ 9,458</b>	<b>\$ 9,458</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>
<b>Operating Expenses</b>								
4	Labor	\$ (24,152)		\$ (14,417)		\$ (9,735)		
5	Purchased Water	\$ -						
6	Fuel & Power	\$ -						
7	Chemicals	\$ -						
8	Waste Disposal	\$ -						
9	Management Fees	\$ (155,753)				\$ (6,514)		
10	Group Insurance	\$ (2,033)					\$ (39,203)	\$ (2,033)
11	Pensions	\$ (39,203)						
12	Regulatory Expense	\$ (27,003)		\$ (27,003)				
13	Insurance Other Than Group	\$ -						
14	Customer Accounting	\$ -						
15	Rents	\$ -						
16	General Office Expense	\$ -						
17	Miscellaneous	\$ (3,250)						
18	Maintenance Expense	\$ -						
19	Depreciation & Amortization	\$ 1,202						
20	General Taxes - Property Taxes	\$ -						
21	General Taxes - Other	\$ -						
15	PRE-TAX OPERATING EXPENSES	\$ (250,193)		\$ (27,003)	\$ (14,417)	\$ (16,249)	\$ (39,203)	\$ (2,033)
16	PRE-TAX OPERATING INCOME	\$ 259,651	\$ 9,458	\$ 27,003	\$ 14,417	\$ 16,249	\$ 39,203	\$ 2,033
17	Income Taxes	\$ 90,292	\$ 3,651	\$ 10,423	\$ 5,565	\$ 6,272	\$ 15,132	\$ 785
18	TOTAL OPERATING EXPENSES	\$ (159,901)	\$ 3,651	\$ (16,580)	\$ (8,852)	\$ (9,977)	\$ (24,071)	\$ (1,248)
19	OPERATING INCOME	\$ 169,359	\$ 5,807	\$ 16,580	\$ 8,852	\$ 9,977	\$ 24,071	\$ 1,248

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C-3 38.60%

Arizona American Water Company - Anthem Water  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	Dues, Donations & Misc. Expenses C-7	Management Fees - Other Expenses C-9	Management Fees - 4% Post-Test Year Wage Increase C-9A	Management Fees - Employee Benefits C-10	Management Fees - Incentive Compensation C-11	Management Fees - Normalize Affiliate Pension Expense C-12
				New			
	<b>Revenues</b>						
1	Water Revenues						
2	Other Revenues						
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
	<b>Operating Expenses</b>						
4	Labor						
5	Purchased Water						
6	Fuel & Power						
7	Chemicals						
8	Waste Disposal						
9	Management Fees		\$ (15,954)	\$ (17,548)	\$ (53,795)	\$ (50,261)	\$ (833)
10	Group Insurance						
11	Pensions						
12	Regulatory Expense						
13	Insurance Other Than Group						
14	Customer Accounting						
15	Rents						
16	General Office Expense						
17	Miscellaneous	\$ (3,250)					
18	Maintenance Expense						
19	Depreciation & Amortization						
20	General Taxes - Property Taxes						
21	General Taxes - Other						
15	PRE-TAX OPERATING EXPENSES	\$ (3,250)	\$ (15,954)	\$ (17,548)	\$ (53,795)	\$ (50,261)	\$ (833)
16	PRE-TAX OPERATING INCOME	\$ 3,250	\$ 15,954	\$ 17,548	\$ 53,795	\$ 50,261	\$ 833
17	Income Taxes	\$ 1,255	\$ 6,158	\$ 6,774	\$ 20,765	\$ 19,401	\$ 322
18	TOTAL OPERATING EXPENSES	\$ (1,995)	\$ (9,796)	\$ (10,774)	\$ (33,030)	\$ (30,860)	\$ (511)
19	OPERATING INCOME	\$ 1,995	\$ 9,796	\$ 10,774	\$ 33,030	\$ 30,860	\$ 511

Notes and Source  
Combined Effective Tax Rate per AAWC filing, Sch. C-3



Arizona American Water Company - Anthem Water  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	Management Fees - Normalize Expense C-13	Management Fees - Remove Business Development Expenses C-14	Interest Synchronization C-15	Depreciation Expense - Anthem Water Reclassified Accounts C-18	New
1	Revenues					
2	Water Revenues					
3	Other Revenues					
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -
4	Operating Expenses					
4	Labor					
5	Purchased Water					
6	Fuel & Power					
7	Chemicals					
8	Waste Disposal					
9	Management Fees	\$ (1,410)	\$ (9,438)			
10	Group Insurance					
11	Pensions					
12	Regulatory Expense					
13	Insurance Other Than Group					
14	Customer Accounting					
15	Rents					
16	General Office Expense					
17	Miscellaneous					
18	Maintenance Expense					
19	Depreciation & Amortization					
20	General Taxes - Property Taxes					
21	General Taxes - Other					
15	PRE-TAX OPERATING EXPENSES	\$ (1,410)	\$ (9,438)	\$ -	\$ -	\$ 1,202
16	PRE-TAX OPERATING INCOME	\$ 1,410	\$ 9,438	\$ -	\$ -	\$ (1,202)
17	Income Taxes	\$ 544	\$ 3,643	\$ (9,934)	\$ (464)	
18	TOTAL OPERATING EXPENSES	\$ (866)	\$ (5,795)	\$ (9,934)	\$ 738	
19	OPERATING INCOME	\$ 866	\$ 5,795	\$ 9,934	\$ (738)	

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C-3

Arizona American Water Company - Sun City Water  
Calculation of Revenue Deficiency (Sufficiency)

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule A (SC)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B (SC)	\$ 28,186,063	\$ 26,215,284	\$ (1,970,779)
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 2,404,271	\$ 1,775,823	\$ (628,448)
4	Adjusted net operating income	C (SC)	\$ 861,085	\$ 1,359,588	\$ 498,503
5	Net operating income deficiency		\$ 1,543,186	\$ 416,235	\$ (1,126,951)
6	Gross revenue conversion factor	A-1 (SC)	1.6402	1.6402	
7	Revenue deficiency (Sufficiency)		\$ 2,531,127	\$ 682,709	\$ (1,848,418)
<b>Percentage Increase Over Current Rates</b>					
8	Revenue from Sales to Retail Customers	Sch C (SC), L.1	\$ 9,125,203	\$ 9,125,203	
9	Percentage Increase	L.7 / L.8	27.74%	7.48%	

Notes and Source

Col.A: AAWC Filing, Schedule A-1

<b>Calculation of RUCO recommended percentage increase to AAWC's base rates</b>			RUCO Proposed
AAWC's adjusted water revenues per Schedule C (SC)			\$ 9,125,203
RUCO recommended rate increase (line 7 above)			\$ 682,709
Total revenues after reflecting RUCO recommended increase			\$ 9,807,912
Percentage change in revenues			7.48%

<b>Calculation of AAWC's proposed percentage increase to base rates</b>			AAWC Proposed
AAWC's adjusted water revenues per Schedule C (SC)			\$ 9,125,203
AAWC proposed rate increase (line 7 above)			\$ 2,531,127
Total revenues after reflecting AAWC proposed increase			\$ 11,656,330
Percentage change in revenues			27.74%

Arizona American Water Company - Sun City Water  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule A-1 (SC)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.34%	0.34%
3	Bad Debt Expense	0.09%	0.09%
4	Taxable Income as a Percent	99.57%	99.57%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.94%	67.94%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.97%	60.97%
9	<b>Gross Revenue Conversion Factor</b>	<b>1.6402</b>	<b>1.6402</b>

Notes and Source

Col.A: AAWC Filing, Schedule C-3

Combined state and federal income tax rate	38.60%	38.60%
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Components of Revenue Requirement Increase

	Amount	Percent
11 Net Income	\$ 416,236	60.97%
12 Federal Income Taxes	\$ 215,947	31.63%
13 State Income Taxes	\$ 47,571	6.97%
14 Property Taxes	\$ 2,330	0.34%
15 Uncollectibles	\$ 625	0.09%
16 Total Revenue Increase	\$ 682,709	100.00%
17 Total Revenue Increase (From Schedule A (SC))	\$ 682,709	

Arizona American Water Company - Sun City Water  
Adjusted Rate Base

Attachment RCS-6  
Schedule B (SC)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 63,616,418	\$ (1,272,682)	\$ 62,343,736
2	Accumulated Depreciation	\$ (18,973,897)	\$ (441,956)	\$ (19,415,853)
3	<b>Net Utility Plant in Service</b>	<b>\$ 44,642,520</b>	<b>\$ (1,714,638)</b>	<b>\$ 42,927,883</b>
<b>Less:</b>				
4	Advances in Aid of Construction	\$ (5,860,651)	\$ -	\$ (5,860,651)
5	Contributions in Aid of Construction (net of amortization)	\$ (13,179,713)	\$ (38,991)	\$ (13,218,704)
6	Imputed Regulatory Advances	\$ -	\$ -	\$ -
7	Imputed Regulatory Contributions	\$ (342,458)	\$ -	\$ (342,458)
8	Customer Meter Deposits	\$ (2,450)	\$ -	\$ (2,450)
9	Deferred Income Taxes and Credits	\$ 1,904,817	\$ (49,151)	\$ 1,855,666
10	Investment Tax Credits and Deferred Credits	\$ -	\$ -	\$ -
11	<b>Total Reductions</b>	<b>\$ (17,480,455)</b>	<b>\$ (88,142)</b>	<b>\$ (17,568,597)</b>
<b>Plus:</b>				
12	Unamortized Finance Charges	\$ -	\$ -	\$ -
13	Deferred Tax Assets	\$ -	\$ -	\$ -
14	Deferred Debits	\$ 437,906	\$ -	\$ 437,906
15	Allowance for Working Capital	\$ 586,091	\$ (168,000)	\$ 418,091
16	Utility Plant Acquisition Adjustment	\$ -	\$ -	\$ -
17	<b>Total Additions</b>	<b>\$ 1,023,997</b>	<b>\$ (168,000)</b>	<b>\$ 855,997</b>
18	<b>Total Rate Base</b>	<b>\$ 28,186,063</b>	<b>\$ (1,970,780)</b>	<b>\$ 26,215,284</b>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1

Arizona American Water Company - Sun City Water  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B.1 (SC)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments	Post-Test Year Plant - Well 5.1 B-1	Contributions in Aid of Construction B-3		Cash Working Capital B-4 Revised	Youngstown Plant B-5		Accumulated Deferred Income Taxes B-9	
				Construction	Aid of Construction		New	New	Deferred	New
1	Gross Utility Plant in Service	\$ (1,272,682)	\$ (1,123,185)					\$ (149,497)		
2	Accumulated Depreciation	\$ (441,956)	\$ (463,964)					\$ 22,008		
3	Net Utility Plant in Service	\$ (1,714,638)	\$ (1,587,149)	\$ -	\$ -	\$ -		\$ (127,489)	\$ -	
<b>Less:</b>										
4	Advances in Aid of Construction	\$ -								
5	Contributions in Aid of Construction (net of amortization)	\$ (38,991)		\$ (38,991)						
6	Imputed Regulatory Advances	\$ -								
7	Imputed Regulatory Contributions	\$ -								
8	Customer Meter Deposits	\$ -								
9	Deferred Income Taxes and Credits	\$ (49,151)							\$ (49,151)	
10	Investment Tax Credits and Deferred Credits	\$ -								
11	Total Reductions	\$ (88,142)	\$ -	\$ (38,991)	\$ -	\$ -		\$ -	\$ (49,151)	
<b>Plus:</b>										
12	Unamortized Finance Charges	\$ -								
13	Deferred Tax Assets	\$ -								
14	Deferred Debits	\$ -								
15	Allowance for Working Capital	\$ (168,000)			\$ (168,000)					
16	Utility Plant Acquisition Adjustment	\$ -								
17	Total Additions	\$ (168,000)	\$ -	\$ -	\$ (168,000)	\$ (168,000)		\$ -	\$ -	
18	Total Rate Base	\$ (1,970,780)	\$ (1,587,149)	\$ (38,991)	\$ (127,489)	\$ (168,000)		\$ (127,489)	\$ (49,151)	

Notes and Source

See referenced exhibit for each adjustment

Arizona American Water Company - Sun City Water  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule C (SC)  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Water Revenues	\$ 9,125,203	\$ -	\$ 9,125,203
2	Other Revenues	\$ 157,898	\$ -	\$ 157,898
3	<b>Total Revenues</b>	<u>\$ 9,283,101</u>	<u>\$ -</u>	<u>\$ 9,283,101</u>
<b>Operating Expenses</b>				
4	Labor	\$ 1,225,670	\$ (31,378)	\$ 1,194,292
5	Purchased Water	\$ -	\$ -	\$ -
6	Fuel & Power	\$ 1,722,582	\$ -	\$ 1,722,582
7	Chemicals	\$ 37,037	\$ -	\$ 37,037
8	Waste Disposal	\$ -	\$ -	\$ -
9	Management Fees	\$ 1,509,322	\$ (202,994)	\$ 1,306,328
10	Group Insurance	\$ 354,396	\$ (2,650)	\$ 351,746
11	Pensions	\$ 251,435	\$ (92,636)	\$ 158,799
12	Regulatory Expense	\$ 75,286	\$ (24,304)	\$ 50,982
13	Insurance Other Than Group	\$ 93,255	\$ -	\$ 93,255
14	Customer Accounting	\$ 235,348	\$ -	\$ 235,348
15	Rents	\$ 60,016	\$ -	\$ 60,016
16	General Office Expense	\$ 78,546	\$ -	\$ 78,546
17	Miscellaneous	\$ 300,084	\$ (4,237)	\$ 295,847
18	Maintenance Expense	\$ 652,601	\$ (445,000)	\$ 207,601
19	Depreciation & Amortization	\$ 1,565,706	\$ (36,961)	\$ 1,528,745
20	General Taxes - Property Taxes	\$ 156,074	\$ -	\$ 156,074
21	General Taxes - Other	\$ 94,912	\$ -	\$ 94,912
22	Income Taxes	\$ 9,746	\$ 341,658	\$ 351,404
23	<b>Total Operating Expenses</b>	<u>\$ 8,422,016</u>	<u>\$ (498,503)</u>	<u>\$ 7,923,513</u>
24	<b>Utility Operating Income</b>	<u>\$ 861,085</u>	<u>\$ 498,503</u>	<u>\$ 1,359,588</u>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -		\$ -
26	Interest Expense	\$ (845,582)		\$ (845,582)
27	Other Expense	\$ (18,348)		\$ (18,348)
28	Gain/Loss Sale of Fixed Assets	\$ (4)		\$ (4)
29	<b>Total Other Additions/Deductions From Income</b>	<u>\$ (863,934)</u>	<u>\$ -</u>	<u>\$ (863,934)</u>
30	<b>Net Profit (Loss)</b>	<u>\$ (2,849)</u>	<u>\$ 498,503</u>	<u>\$ 495,654</u>
31	Rate Base	<u>\$ 28,186,063</u>	<u>\$ (1,970,780)</u>	<u>\$ 26,215,283</u>
32	Earned Rate of Return	<u>3.06%</u>		<u>5.19%</u>

Notes and Source

Col.A: AAWC Filing, Schedule C-1  
Col.B: Schedule C.1  
Col.C: Col.A + Col.B

Arizona American Water Company - Sun City Water  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-6  
Schedule C.1 (SC)  
Docket No. W-01303A-09-0343  
Page 1 of 3  
Revised

Attachment RCS-6  
Docket No. W-01303A-09-0343  
Page 25 of 53

Line No.	Description	RUCO Adjustments	Rate Case Expense C-2	Achievement Incentive Pay C-3	Stock-Based Compensation C-4	Pension Expense C-5	OPEB Expense C-6	Dues, Donations & Misc. Expenses C-7
	<b>Revenues</b>							
1	Water Revenues	\$ -						
2	Other Revenues	\$ -						
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
	<b>Operating Expenses</b>							
4	Labor	\$ (31,378)		\$ (18,690)	\$ (12,688)			
5	Purchased Water	\$ -						
6	Fuel & Power	\$ -						
7	Chemicals	\$ -						
8	Waste Disposal	\$ -						
9	Management Fees	\$ (202,994)			\$ (8,490)			
10	Group Insurance	\$ (2,650)						
11	Pensions	\$ (92,636)				\$ (92,636)		
12	Regulatory Expense	\$ (24,304)	\$ (24,304)					
13	Insurance Other Than Group	\$ -						
14	Customer Accounting	\$ -						
15	Rents	\$ -						
16	General Office Expense	\$ -						
17	Miscellaneous	\$ (4,237)						\$ (4,237)
18	Maintenance Expense	\$ (445,000)						
19	Depreciation & Amortization	\$ (36,961)						
20	General Taxes - Property Taxes	\$ -						
21	General Taxes - Other	\$ -						
15	PRE-TAX OPERATING EXPENSES	\$ (840,161)	\$ (24,304)	\$ (18,690)	\$ (21,178)	\$ (92,636)	\$ (2,650)	\$ (4,237)
16	PRE-TAX OPERATING INCOME	\$ 840,161	\$ 24,304	\$ 18,690	\$ 21,178	\$ 92,636	\$ 2,650	\$ 4,237
17	Income Taxes	\$ 341,658	\$ 9,381	\$ 7,214	\$ 8,175	\$ 35,758	\$ 1,023	\$ 1,635
18	TOTAL OPERATING EXPENSES	\$ (498,503)	\$ (14,923)	\$ (11,476)	\$ (13,003)	\$ (56,878)	\$ (1,627)	\$ (2,602)
19	OPERATING INCOME	\$ 498,503	\$ 14,923	\$ 11,476	\$ 13,003	\$ 56,878	\$ 1,627	\$ 2,602

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C-3

38.60%

Arizona American Water Company - Sun City Water  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-6  
Schedule C.1 (SC)  
Docket No. W-01303A-09-0343  
Page 2 of 3  
Revised

Attachment RCS-6  
Docket No. W-01303A-09-0343  
Page 26 of 53

Line No.	Description	Management										Management	
		Tank Maintenance Expense	Management Fees - Other Expenses	Management Fees - 4% Post-Test Year Wage Increase	Management Fees - Employee Benefits	Management Fees - Incentive Compensation	Management Fees - Normalize Affiliate Pension Expense	Management Fees - Normalize Affiliate OPEB Expense	C-9A New			C-12	C-13
		C-8	C-9		C-10	C-11							
<b>Revenues</b>													
1	Water Revenues												
2	Other Revenues												
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -				\$ -	\$ -
<b>Operating Expenses</b>													
4	Labor												
5	Purchased Water												
6	Fuel & Power												
7	Chemicals												
8	Waste Disposal												
9	Management Fees		\$ (20,793)	\$ (22,871)	\$ (70,111)	\$ (65,506)	\$ (1,086)	\$ (1,838)					
10	Group Insurance												
11	Pensions												
12	Regulatory Expense												
13	Insurance Other Than Group												
14	Customer Accounting												
15	Rents												
16	General Office Expense												
17	Miscellaneous												
18	Maintenance Expense												
19	Depreciation & Amortization												
20	General Taxes - Property Taxes												
21	General Taxes - Other												
15	PRE-TAX OPERATING EXPENSES	\$ (445,000)	\$ (20,793)	\$ (22,871)	\$ (70,111)	\$ (65,506)	\$ (1,086)	\$ (1,838)					
16	PRE-TAX OPERATING INCOME	\$ 445,000	\$ 20,793	\$ 22,871	\$ 70,111	\$ 65,506	\$ 1,086	\$ 1,838					
17	Income Taxes	\$ 171,770	\$ 8,026	\$ 8,828	\$ 27,063	\$ 25,285	\$ 419	\$ 709					
18	TOTAL OPERATING EXPENSES	\$ (273,230)	\$ (12,767)	\$ (14,043)	\$ (43,048)	\$ (40,221)	\$ (667)	\$ (1,129)					
19	OPERATING INCOME	\$ 273,230	\$ 12,767	\$ 14,043	\$ 43,048	\$ 40,221	\$ 667	\$ 1,129					

\$ (445,000)

Notes and Source  
Combined Effective Tax Rate per AAWC filing, Sch. C



Arizona American Water Company - Sun City Water  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-6  
Schedule C.1 (SC)  
Docket No. W-01303A-09-0343  
Page 3 of 3  
Revised

Attachment RCS-6  
Docket No. W-01303A-09-0343  
Page 27 of 53

Line No.	Description	Management Fees - Remove Business Development Expenses C-14	Interest Synchronization C-15 Revised	Depreciation Expense Related to Post-Test Year Plant - Well 5.1 - Sun City Water C-16
<b>Revenues</b>				
1	Water Revenues			
2	Other Revenues			
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -
<b>Operating Expenses</b>				
4	Labor			
5	Purchased Water			
6	Fuel & Power			
7	Chemicals			
8	Waste Disposal			
9	Management Fees	\$ (12,301)		
10	Group Insurance			
11	Pensions			
12	Regulatory Expense			
13	Insurance Other Than Group			
14	Customer Accounting			
15	Rents			
16	General Office Expense			
17	Miscellaneous			
18	Maintenance Expense			
19	Depreciation & Amortization			\$ (36,961)
20	General Taxes - Property Taxes			
21	General Taxes - Other			
15	<b>PRE-TAX OPERATING EXPENSES</b>	\$ (12,301)	\$ -	\$ (36,961)
16	<b>PRE-TAX OPERATING INCOME</b>	\$ 12,301	\$ -	\$ 36,961
17	Income Taxes	\$ 4,748	\$ 17,357	\$ 14,267
18	<b>TOTAL OPERATING EXPENSES</b>	\$ (7,553)	\$ 17,357	\$ (22,694)
19	<b>OPERATING INCOME</b>	\$ 7,553	\$ (17,357)	\$ 22,694

Notes and Source

Combined Effective Tax Rate per AAWC filing, Sch. C

Arizona American Water Company  
Post-Test Year Additions to Plant - Well 5.1 - Sun City Water

Attachment RCS-6  
Schedule B-1  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Sun City Water	Reference
		(A)	
1	Remove Well 5.1 From Utility Plant in Service	\$ (1,587,149)	A
2	Reverse Retirement of Old Well	\$ 463,964	A&B
3	Gross Utility Plant in Service	<u>\$ (1,123,185)</u>	
3	Increase Accumulated Depreciation for Old Well	<u>\$ (463,964)</u>	B
4	Net Adjustment to Utility Plant in Service	<u>\$ (1,587,149)</u>	

Notes and Source

A: Amounts per Schedule B-2, Adjustment No. LJG-5 from AAWC filing

B: Page 5 of the direct testimony of Company witness Linda J. Gutowski stated:

"The retirement of \$463,964 for the old Well #5.1 was deducted from plant and from accumulated depreciation"

Arizona American Water Company  
Contributions In Aid of Construction

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B-3  
Docket No. W/SW-01303A-09-0343  
Page 1 of 1

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Anthem/ Agua Fria Wastewater (C)	Sun City Wastewater (D)	Sun City West Wastewater* (E)	Total (F)	Reference
1	Reverse Company Adjustments to CIAC	\$ (30,271)	\$ (38,991)	\$ (65,490)	\$ (3,743)	\$ -	\$ (138,495)	A
2	Subtotal Water						\$ (69,262)	
3	Subtotal Wastewater						\$ (69,233)	
4	Total Adjustment						<u>\$ (138,495)</u>	

Notes and Source

A: Per Schedule B-2, Adjustment No. SLM-8 from AAWC filing

\* The Company's adjustment to CIAC related to Sun City West Wastewater netted to zero

Arizona American Water Company  
Cash Working Capital

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule B-4  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Cash Working Capital Requirement Per Filing	\$ 75,089	\$ 416,111	\$ 491,200	A
2	RUCO Recommended Cash Working Capital Requirement	\$ (47,072)	\$ 248,433	\$ 201,361	B
3	Adjustment to Cash Working Capital	\$ (122,161)	\$ (167,678)	\$ (289,839)	
4	Adjustment to Cash Working Capital Rounded to Nearest \$000	\$ (122,000)	\$ (168,000)	\$ (290,000)	

Notes and Source

A: AAWC filing, Schedule B-6

B: See Schedules B-4 (A) and B-4 (SC)

Test Year Ended December 31, 2008

Line No.	Test Year Adjusted Results (A)	RUCO Adjustments (B)	RUCO Adjusted (C)	Revenue Lag Days (D)	Expense Lag Days (E)	Net Lag Days (F)	Lead/Lag Factor (G)	Cash Working Capital Required (H)	Reference
<b>OPERATING EXPENSES</b>									
1	\$ 754,087	\$ (24,152)	\$ 729,935	40.02	12.00	28.02	0.0768	\$ 56,043	
2	\$ 625,435	\$	\$ 625,435	40.02	50.92	-10.89	(0.0298)	\$ (18,664)	
3	\$ 1,259,637	\$	\$ 1,259,637	40.02	22.70	17.33	0.0475	\$ 59,801	
4	\$ 103,351	\$	\$ 103,351	40.02	8.73	0.00	-	\$ -	b
5	\$ 1,933	\$	\$ 1,933	40.02	4.55	35.47	0.0972	\$ 188	
6	\$ 1,158,078	\$ (155,753)	\$ 1,002,325	40.02	12.00	28.02	0.0768	\$ 76,957	a
7	\$ 209,326	\$ (2,033)	\$ 207,293	40.02	-13.70	53.73	0.1472	\$ 30,513	
8	\$ 105,808	\$ (39,203)	\$ 66,605	40.02	-2.37	42.39	0.1161	\$ 7,736	
9	\$ 71,553	\$	\$ 71,553	40.02	-83.68	123.71	0.3389	\$ 24,251	
10	\$ 183,101	\$	\$ 183,101	40.02	20.31	19.71	0.0540	\$ 9,889	c
11	\$ 33,826	\$	\$ 33,826	40.02	0.00	40.02	0.1097	\$ 3,709	
12	\$ 229,300	\$	\$ 229,300	40.02	8.89	31.13	0.0853	\$ 19,556	
13	\$ 140,803	\$	\$ 140,803	40.02	33.61	6.41	0.0176	\$ 2,474	
14	\$ 124,533	\$ (30,253)	\$ 94,280	40.02	30.00	10.02	0.0275	\$ 2,589	
15	\$ 288,011	\$	\$ 288,011	40.02	191.29	-151.27	(0.4144)	\$ (119,363)	
16	\$ 34,882	\$	\$ 34,882	40.02	13.35	26.68	0.0731	\$ 2,550	
17	\$ 1,996,536	\$ 2,134,653	\$ 4,131,189	40.02	30.13	9.89	0.0271	\$ 111,984	
18	\$ 1,722,960	\$ 25,736	\$ 1,748,695	40.02	106.25	-66.23	(0.1814)	\$ (317,285)	
19	\$ 9,043,161	\$ 1,908,994	\$ 10,952,155						

20 Working Cash Requirement  
21 Working Cash Requirement per Company  
22 Adjustment to Cash Working Capital

\$ (47,072)  
\$ 75,089  
\$ (122,161)

Notes and Source

AAWC Filing, Schedule B-6

Col. D: RUCO recommending revenue lag days of 40.02. Company used 46.11 revenue lag days

a: RUCO recommending 12 expense lag days for management fees. Company used 14.77 expense lag days

b: The Company accepted Staff's adjustment to remove chemical expense from its CWC calculation

c: The Company accepted Staff's adjustment to remove bad debt expense from Customer Accounting Expense

Line 17, Col. C, Current Income Taxes:

23 Per AAWC \$ 1,996,536  
24 RUCO adjustments to current income taxes \$ 90,292 Schedule C.1 (A), line 17  
25 Income Taxes for Revenue Increase \$ 2,044,361 Schedule A-1 (A), lines 12 & 13  
26 Total current income taxes for CWC calculation \$ 4,131,189

Test Year Ended December 31, 2008

Line No.	Test Year Adjusted Results (A)	RUCO Adjustments (B)	RUCO Adjusted (C)	Revenue Lag Days (D)	Expense Lag Days (E)	Net Lag Days (F)	Lead/Lag Factor (G)	Working Capital Required (H)	Reference
<b>OPERATING EXPENSES</b>									
1 P08 Labor	\$ 1,225,670	\$ (31,378)	\$ 1,194,292	39.65	12.00	27.65	0.0757	\$ 90,455	
2 P09 Purchased Water	\$ -	\$ -	\$ -	39.65	(59.03)	98.67	0.2703	\$ -	
3 P10 Fuel & Power	\$ 1,722,582	\$ -	\$ 1,722,582	39.65	22.09	17.56	0.0481	\$ 82,858	
4 P11 Chemicals	\$ 37,037	\$ -	\$ 37,037	39.65	15.09	-	-	\$ -	b
5 P12 Waste disposal	\$ -	\$ -	\$ -	39.65	-	39.65	0.1086	\$ -	
6 P13 Management Fees	\$ 1,509,322	\$ (202,994)	\$ 1,306,328	39.65	12.00	27.65	0.0757	\$ 98,941	a
7 P14 Group Insurance	\$ 354,396	\$ (2,650)	\$ 351,746	39.65	(13.70)	53.35	0.1462	\$ 51,412	
8 P15 Pensions	\$ 251,435	\$ (92,636)	\$ 158,799	39.65	(2.37)	42.01	0.1151	\$ 18,279	
9 P17 Insurance Other Than Group	\$ 93,255	\$ -	\$ 93,255	39.65	(83.68)	123.33	0.3379	\$ 31,510	
10 P18 Customer Accounting	\$ 235,348	\$ -	\$ 235,348	39.65	20.31	19.34	0.0530	\$ 12,467	c
11 P19 Rents	\$ 60,016	\$ -	\$ 60,016	39.65	32.82	6.82	0.0187	\$ 1,122	
12 P21 Miscellaneous	\$ 300,084	\$ -	\$ 300,084	39.65	25.96	13.69	0.0375	\$ 11,253	
13 P25 Maintenance Expense	\$ 652,601	\$ (445,000)	\$ 207,601	39.65	23.25	16.40	0.0449	\$ 9,325	
14 Other Operating Expenses	\$ 153,833	\$ (28,541)	\$ 125,292	39.65	30.00	9.65	0.0264	\$ 3,311	
15 P29 Property Taxes	\$ 156,074	\$ -	\$ 156,074	39.65	190.63	(150.99)	(0.4137)	\$ (64,561)	
16 P29 Taxes Other than Income	\$ 94,912	\$ -	\$ 94,912	39.65	13.35	26.30	0.0721	\$ 6,839	
17 P30 Income Tax	\$ 979,846	\$ 605,176	\$ 1,585,022	39.65	30.13	9.52	0.0261	\$ 41,319	
18 P56 Interest	\$ 845,582	\$ (44,967)	\$ 800,615	39.65	106.25	(66.61)	(0.1825)	\$ (146,096)	
19 Total	\$ 8,671,993	\$ (242,991)	\$ 8,429,002					\$ 248,433	
20 Working Cash Requirement								\$ 416,111	
21 Working Cash Requirement per Company								\$ (167,678)	
22 Adjustment to Cash Working Capital									

Notes and Source  
AAWC Filing, Schedule B-6

Col. D: RUCO recommending revenue lag days of 39.65. Company used 45.73 revenue lag days  
a: RUCO recommending 12 expense lag days for management fees. Company used 14.77 expense lag days  
b: The Company accepted Staff's adjustment to remove chemical expense from its CWC calculation  
c: The Company accepted Staff's adjustment to remove bad debt expense from Customer Accounting Expense

Line 17, Col. C. Current Income Taxes:	
23 Per AAWC	\$ 979,846
24 RUCO adjustments to current income taxes	\$ 341,658
25 Income Taxes for Revenue Increase	\$ 263,518
26 Total current income taxes for CWC calculation	\$ 1,585,022

Line No.	Description	Sun City Water	Reference
		(A)	
1	Adjustment to Reduce Utility Plant in Service Related to Youngstown Plant	\$ (149,497)	A
2	Adjustment to Reduce Accumulated Depreciation Related to Youngstown Plant	\$ 22,008	A
3	Net Adjustment to Utility Plant in Service	<u>\$ (127,489)</u>	

Notes and Source

A: AAWC accepted Staff's adjustment related to the Youngtown Plant per the rebuttal testimony of Company witness Sandra L. Murrey

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Anthem/ Agua Fria Wastewater (C)	Sun City Wastewater (D)	Sun City West Wastewater (E)	Total (F)	Reference
1	Adjustment to Reduce Accumulated Deferred Income Taxes	\$ (18,580)	\$ (49,151)	\$ (27,084)	\$ (47,073)	\$ (32,077)	\$ (173,965)	A
2	Subtotal Water						\$ (67,731)	
3	Subtotal Wastewater						\$ (106,234)	
4	Total Adjustment						\$ (173,965)	

Notes and Source

A: AAWC accepted Staff's adjustments to ADIT per the rebuttal testimony of Company witness Linda J. Gutowski



Arizona American Water Company  
Customer Annualization Correction - Anthem Water

Test Year Ended December 31, 2008

Attachment RCS-6  
Schedule C-1  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Anthem Water	Reference
1	Adjustment to Increase Annualized Revenue to Reflect Error Correction	\$ 9,458	A

Notes and Source

A: Company witness Linda J. Gutowski stated in her Rebuttal Testimony that the correction of the error in the customer annualization adjustment increases water revenue for the Anthem Water district

Arizona American Water Company  
Rate Case Expense

Attachment RCS-6  
Schedule C-2  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Estimated Normalized Rate Case Expense Per Filing	\$ 57,546	\$ 63,081	\$ 120,627	A
2	RUCO Recommended Normalized Rate Case Expense	\$ 30,543	\$ 38,777	\$ 69,320	B
3	Adjustment to Rate Case Expense	\$ (27,003)	\$ (24,304)	\$ (51,307)	L2 - L1

Notes and Source

A: AAWC estimated normalized rate case expense calculated as follows (amounts from Adjustment MHK-8 from AAWC filing):

	Anthem Water	Sun City Water
4 Estimated Rate Case Expense per Company	\$ 678,425	\$ 678,425
5 Normalized over three years	3	3
6 Estimated Normalized Rate Case Expense	\$ 226,142	\$ 226,142
7 2009 Group 4-Factor per Company	19.919%	25.289%
8 Allocated Rate Case Expense	\$ 45,046	\$ 57,190
9 Unamortized Balance of Prior Rate Case Expense	\$ 37,500	\$ 17,674
10 Normalized over three years	3	3
11 Annual Amortization of Unamortized Rate Case Expense	\$ 12,500	\$ 5,891
12 Pro Forma Rate Case Expense	\$ 57,546	\$ 63,081

B: RUCO recommended Rate Case Expense calculated as follows:

13 RUCO recommended Rate Case Expense	\$ 460,000	\$ 460,000
14 Normalized over three years	3	3
15 Normalized Rate Case Expense	\$ 153,333	\$ 153,333
16 2009 Group 4-Factor	19.919%	25.289%
17 Allocated Rate Case Expense	\$ 30,543	\$ 38,777

Arizona American Water Company  
Achievement Incentive Pay

Attachment RCS-6  
Schedule C-3  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Achievement Incentive Pay Recorded at 12/31/2008	\$ 3,496	\$ 4,224	\$ 7,720	A
2	Corporate Allocation	\$ 44,560	\$ 58,075	\$ 102,635	A&B
3	Total Achievement Incentive Pay	\$ 48,056	\$ 62,299	\$ 110,355	
4	Disallowance Percentage	30%	30%		C
5	Adjustment to Achievement Incentive Pay	\$ (14,417)	\$ (18,690)	\$ (33,107)	

Notes and Source

- A: Amounts above per Company workpaper "AI-2008" for each district  
B: Corporate allocation amounts also provided in AAWC's responses to RUCO 2-6 and RUCO 3-2  
C: Testimony of RUCO witness Ralph Smith

Arizona American Water Company  
Stock-Based Compensation

Attachment RCS-6  
Schedule C-4  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Adjustment to Remove Stock-Based Compensation - Management Fees	\$ (6,514)	\$ (8,490)	\$ (15,004)	A
2	Adjustment to Remove Stock-Based Compensation - Labor	\$ (9,735)	\$ (12,688)	\$ (22,423)	A
3	Total Adjustment to Remove Stock-Based Compensation	<u>\$ (16,249)</u>	<u>\$ (21,178)</u>	<u>\$ (37,427)</u>	

Notes and Source

A: Amounts below from AAWC's supplemental response to RUCO 6-3

Description	Service Company Portion	AAWC Non-Affiliate Portion	Total
4 Comp - Stock Options - Account 501716	\$ 36,693		\$ 36,693
5 Comp - Restricted Stock - Account 501717	\$ 28,834	\$ 103,974	\$ 132,808
6 Comp - Restricted Stock Units - Account 701718	\$ 4,046		\$ 4,046
7 Total Test Year Stock-Based Compensation	<u>\$ 69,573</u>	<u>\$ 103,974</u>	<u>\$ 173,547</u>

Service Company Portion

8 Total Test Year Stock-Based Compensation - Service Company Portion	\$ 69,573	\$ 69,573
9 4 Factor Allocator	9.3634%	12.2033%
10 Total Allocated Test Year Stock-Based Compensation - Service Company Portion	<u>\$ 6,514</u>	<u>\$ 8,490</u>

Non-Affiliate Portion

11 Total Test Year Stock-Based Compensation - Non-Affiliate Portion	\$ 103,974	\$ 103,974
12 4 Factor Allocator	9.3634%	12.2033%
13 Total Allocated Test Year Stock-Based Compensation - Non-Affiliate Portion	<u>\$ 9,735</u>	<u>\$ 12,688</u>

Arizona American Water Company  
Pension Expense

Attachment RCS-6  
Schedule C-5  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Pro Forma Pension Expense Per Filing	\$ 120,860	\$ 267,828	\$ 388,689	A
2	RUCO Recommended Pro Forma Pension Expense	\$ 81,657	\$ 175,192	\$ 256,849	B&C
3	Adjustment to Pension Expense	\$ (39,203)	\$ (92,636)	\$ (131,839)	

Notes and Source

A: Per Schedule C-2, Adjustment No. SLH-2 from AAWC's filing

B: RUCO recommended pension expense calculated as follows (amounts from AAWC's response to RUCO 2-60):

	Amount
5 Recorded Pension Expense - 2007	\$ 903,222
6 Recorded Pension Expense - 2008	\$ 1,734,561
7 Subtotal	\$ 2,637,783
8 Normalized Over Two Years	2
9 Normalized Pension Expense	\$ 1,318,892

C: RUCO calculated its pension expense adjustment by incorporating the normalized amount above to Company worksheet "AZ 2008 Labor" as shown on pages 2 and 3 of this schedule

A	B	C	D	E	F	G	H	I	J	K	L	
115	ARIZONA-AMERICAN WATER COMPANY						Exhibit					
116	SUMMARY OF PENSION PRO FORMA ADJUSTMENTS						Schedule C-2					
117	TEST YEAR ENDED DECEMBER 31, 2008						Page					
118							Witness: Hubbard					
Line No.	District	Business Unit	RUCO	Adjusted Test Year Pension Expense	Test Year Pension Expense	Difference	Per AAWC Adjusted Test Year Pension Expense	Per RUCO Pension Expense	RUCO Adjustment			
121												
122	1											
123	2 Anthem Water	2381, 2383	\$	81,657.13	\$	162,414.00	\$	120,860.39	\$	81,557.13	\$	135,203.26
124	3											
125	4											
126	5											
127	6											
128	7 Sun City Water	2362	\$	175,192.00	\$	211,674.00	\$	267,828.16	\$	175,192.00	\$	191,616.15
129	8											
130	9											
131	10											
132	11											
133	12 Anthem Wastewater	2382, 2384	\$	70,701.52	\$	100,380.00	\$	106,761.98	\$	70,701.52	\$	136,060.45
134	13											
135	14											
136	15											
137	16											
138	17 Agua Fria Wastewater	2385	\$	56,670.94	\$	113,914.00	\$	81,710.83	\$	56,670.94	\$	125,039.89
139	18 Northwest Valley Regional Treatment Facility @ 32%	2346	\$	21,784.85	\$		\$	31,167.49	\$	21,784.85	\$	111,387.64
140	19 Total Agua Fria Wastewater		\$	78,455.79	\$	113,914.00	\$	114,878.32	\$	78,455.79	\$	136,427.33
141	20											
142	21											
143	22											
144	23											
145	24 Sun City Wastewater	2363	\$	49,093.81	\$	130,870.00	\$	74,280.77	\$	49,093.81	\$	125,186.96
146	25											
147	26											
148	27											
149	28											
150	29 Sun City West Wastewater	2365	\$	51,667.97	\$	110,737.00	\$	78,489.93	\$	51,667.97	\$	126,821.96
151	30 Northwest Valley Regional Treatment Facility @ 68%	2346	\$	46,292.81	\$		\$	70,480.92	\$	46,292.81	\$	124,188.11
152	31 Total Sun City West Wastewater		\$	97,960.78	\$	110,737.00	\$	148,970.85	\$	97,960.78	\$	151,010.07
153	32											
154	33 Total All Districts		\$	553,061.04	\$	829,989.00	\$	833,580.46	\$	553,061.04	\$	1,280,519.43
155	34											
156	35											
157	36											
158	37											
159	38											
160	39											
161	40											
162	41											
163	42											
164	43											
165	44											
166	45 Workpapers & Supporting Documents:											
167	46 09 Sun City West Wastewater(Sun City West Wastewater)@ 68%											
168	47 10Sun City West Wastewater(Sun City West Wastewater)@ 68%											
169	48											

Cases\AZ RUCO AZ American Water 2009\Testimony\AZ 2008 Labor\_Pension\_Adjustment.xlsx[Sheet1]

Arizona American Water Company  
Test Year Ending December 31, 2008  
Pension Expense

Line No.	Average Recorded Pension, 2007-2008	\$ 1,318,892
1		
2		
3	Number of Active Participants	107
4		
5	Average Cost per Participant	\$ 12,326
6		
7	Average Cost Per Participant Per Hour (ln. 5 + 2,080 hrs.)	\$ 5.93
8		
9	Compare per AWWC:	
10	Actual Pension Funding Expense for 2009 under ERISA	\$ 2,090,643 = '2008 Pension ID89
11	Total reduction L1 - L10	\$ (771,751)
12		
13		
14		
15		
16		
17		
18		
19		
20	Defined Contribution Plan for new Hires beginning 1/1/06	
21	Beginning 1/1/06, the Company no longer offers a Pension Plan to new hires.	
22	Instead, new hires get the Defined Contribution Plan as a benefit.	
23	The Company will contribute 5.25% of Base Pay into a Defined Contribution Plan.	
24		
25	New Hires after 1/1/2006	Base Pay 5.25% \$207,588
26		
27	Number of Active Participants	79
28		
29	Average Cost per Participant	\$2,627.70
30		
31	Average Cost Per Participant Per Hour (Ln.27 + 2,080 hrs.)	\$ 1.26
32		
33		
34		
35		

AZ 2008 Labor\_Pension Adjustment Pension

Arizona American Water Company  
OPEB Expense

Attachment RCS-6  
Schedule C-6  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Normalized OPEB Expense Per Filing (Expensed Portion)	\$ 78,238	\$ 78,238		A
2	4 Factor Allocation Factor	9.363%	12.203%		
3	Adjusted Test Year OPEB Expense Per Company	\$ 7,326	\$ 9,548	\$ 16,874	
4	RUCO Recommended Pro Forma OPEB Expense	\$ 5,293	\$ 6,898	\$ 12,191	
5	Adjustment to OPEB Expense	\$ (2,033)	\$ (2,650)	\$ (4,683)	

Notes and Source

A: Per Schedule C-2, Adjustment No. SLH-14 from AAWC's filing

B: RUCO recommended pension expense calculated as follows (amounts from AAWC's response to RUCO 2-60):

	Amount
7 Recorded OPEB Cost - 2007	\$ 62,603
8 Recorded OPEB Cost - 2008	\$ 75,723
9 Subtotal	\$ 138,326
10 Normalized Over Two Years	2
11 Normalized OPEB Cost	\$ 69,163
12 Capitalization Percentage	18.3%
13 Capitalized Portion of OPEB Cost	\$ (12,634)
14 Expensed Portion of OPEB Cost	\$ 56,529
	L11 + L13
15 4 Factor Allocation Factor	9.363%
16 Anthem Water Portion of OPEB Expense	\$ 5,293
	L14 x L15
17 4 Factor Allocation Factor	12.203%
18 Sun City Water Portion of OPEB Expense	\$ 6,898
	L14 x L17



Test Year Ended December 31, 2008

Line No.	Description	Anthem Water 9.3634%	Sun City Water 12.2033%	Anthem/ Agua Fria Wastewater 12.3543%	Sun City Wastewater 7.5448%	Sun City West Wastewater 6.3842%	Total 47.8500%	Reference
		(A)	(B)	(C)	(D)	(E)	(F)	
1	Membership Dues	\$ (1,774)	\$ (2,313)	\$ (2,341)	\$ (1,430)	\$ (1,210)	\$ (9,068)	A
2	Charitable Contributions	\$ (796)	\$ (1,038)	\$ (1,051)	\$ (642)	\$ (543)	\$ (4,070)	A
3	Community Relations	\$ (504)	\$ (657)	\$ (665)	\$ (406)	\$ (343)	\$ (2,575)	A
4	Advertising Expense	\$ (176)	\$ (229)	\$ (232)	\$ (142)	\$ (120)	\$ (899)	A
5	Total	\$ (3,250)	\$ (4,237)	\$ (4,289)	\$ (2,620)	\$ (2,216)	\$ (16,612)	
6	Subtotal Water						\$ (7,487)	
7	Subtotal Wastewater						\$ (9,125)	
8	Total Adjustment						\$ (16,612)	

Notes and Source

A: Amounts per AAWC's response to RUCO 2-43

	Amount
9 Membership Dues	\$ 18,951
10 Charitable Contributions	\$ 8,505
11 Community Relations	\$ 5,380
12 Advertising Expense	\$ 1,880
13 Total	\$ 34,716

see below

Breakout of Advertising Expenses being removed:

14 Public Works Financing - Corporate	\$ 594
15 Hanley Wood LLC - Marketing	\$ 318
16 Hanley Wood LLC - Marketing	\$ 636
17 Naylor LLC - Marketing	\$ 295
18 Identity Links, Inc. - Promotional	\$ 8
19 Langa Resource Group-REMIT - Promotional	\$ 19
20 M&N Services LLC - Promotional	\$ 10
21 Total	\$ 1,880

Arizona American Water Company  
 Tank Maintenance Expense - Sun City Water

Attachment RCS-6  
 Schedule C-8  
 Docket No. W-01303A-09-0343  
 Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Sun City		Reference
		Water	(A)	
1	Adjusted Test Year Tank Maintenance Expense Per Filing	\$	475,201	. A
2	Adjustment to Remove Proposed Accrual for Deferred Tank Maintenance	\$	(445,000)	
3	RUCO Recommended Tank Maintenance Expense	\$	<u>30,201</u>	

Notes and Source

A: Per Sun City Water, Schedule C-2, page 29, Adjustment No. SLH-11 from Arizona-American filing

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Anthem/Agua Fria Wastewater (C)	Sun City Wastewater (D)	Sun City West Wastewater (E)	Total (F)	Reference
1	Reverse AAWC Adjustment to Annualize Management Fees - Other Expenses	\$ (15,954)	\$ (20,793)	\$ (21,050)	\$ (12,855)	\$ (10,878)	\$ (81,530)	A
2	Subtotal Water						\$ (36,747)	
3	Subtotal Wastewater						\$ (44,783)	
4	Total Adjustment						\$ (81,530)	

Notes and Source

A: Per Schedule C-2, Adjustment No. MHK-4 from AAWC filing

Arizona American Water Company  
Management Fees - Remove AAWC's Requested Post Test Year Increase in Affiliate Employee Benefits

Attachment RCS-6  
Schedule C-10  
Docket No. W-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water 9.3634%	(A)	Sun City Water 12.2033%	(B)	Anthem/ Agua Fria Wastewater 12.3543%	(C)	Sun City Wastewater 7.5448%	(D)	Sun City West Wastewater 6.3842%	(E)	Total 47.8500%	(F)	Reference
Remove AAWC's 22.22% Post Test Year Increase in Employee Benefits														
1	Per AAWC	\$ 71,343	\$ 92,981	\$ 94,132	\$ 57,487	\$ 48,643	\$ 364,587							A
2	Per RUCO	\$ 17,548	\$ 22,871	\$ 23,154	\$ 14,140	\$ 11,965	\$ 89,678							B
3	Adjustment	\$ (53,795)	\$ (70,111)	\$ (70,978)	\$ (43,347)	\$ (36,678)	\$ (274,909)							
4	Subtotal Water						\$ (123,905)							
5	Subtotal Wastewater						\$ (151,004)							
6	Total Adjustment						\$ (274,909)							

Notes and Source

- A Per Schedule C-2, Adjustment No. MHK-3 from AAWC filing  
B Allows 4 percent March 2009 pay increase and removes AAWC's requested 22% post test year increase in employee benefits

Line No.	Description	Remove AAWC's 22.22% Post Test Year Increase in Employee Benefits										Reference
		(A)	(B)	(C)	(D)	(E)	(F)					
	Anthem Water	9.3634%	Sun City Water	12.2033%	Anthem/ Agua Fria Wastewater	12.3543%	Sun City Wastewater	7.5448%	Sun City West Wastewater	6.3842%	Total	47.8500%
1	Per AAWC	\$ 50,261	\$ 65,506	\$ 66,317	\$ 40,500	\$ 34,269	\$ 256,853					A
2	Per RUCO	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -					B
3	Adjustment	\$ (50,261)	\$ (65,506)	\$ (66,317)	\$ (40,500)	\$ (34,269)	\$ (256,853)					
4	Subtotal Water						\$ (115,767)					
5	Subtotal Wastewater						\$ (141,086)					
6	Total Adjustment						\$ (256,853)					

Notes and Source

A Derived from Company's response to RUCO 4-3

Account	Description	Test Year Total Recorded	4% Pay Increase	Total Incentive Comp Removal
501711	Incentive Plan-Off-Annual	\$ 497,594	\$ 8,155	\$ 505,749
501712	Incentive Plan-Off-Long Term	\$ 30,538	\$ 500	\$ 31,038
	Totals	\$ 528,132	\$ 8,655	\$ 536,787

B Reflects removal of all affiliate incentive compensation expense to AWWC in the test year

Attachment RCS-6  
Schedule C-12  
Docket Nos. WSW-01303A-09-0343  
Page 1 of 1

Arizona American Water Company  
Management Fees - Normalize Affiliate Pension Expense  
Test Year Ended December 31, 2008

Line No.	Description	Anthem Water 9.3634% (A)	Sun City Water 12.2033% (B)	Anthem/ Agua Fria Wastewater 12.3543% (C)	Sun City Wastewater 7.5448% (D)	Sun City West Wastewater 6.3842% (E)	Total 47.8500% (F)	Reference
1	Per AWWC	\$ 46,779	\$ 60,967	\$ 61,722	\$ 37,694	\$ 31,895	\$ 239,057	A
2	Per RUCO	\$ 45,946	\$ 59,881	\$ 60,623	\$ 37,022	\$ 31,327	\$ 234,800	B
3	Adjustment	\$ (833)	\$ (1,086)	\$ (1,099)	\$ (671)	\$ (568)	\$ (4,257)	
4	Subtotal Water						\$ (1,919)	
5	Subtotal Wastewater						\$ (2,338)	
6	Total Adjustment						\$ (4,257)	

Normalize Affiliate Pension Expense in Management Fees:

Account	Description	Test Year Total Recorded	4% Pay Increase	Total Incentive Comp Removal
506100	Pension	\$ 491,541	\$ 8,056	\$ 499,596
506100	Pension	\$ 491,541		

Compare amounts from Company's response to RUCO 4-5, Service Company Charges by Object Account (O&M):

Year	Amount	Reference
2007	\$ 489,857	RUCO 4-5
2008	\$ 491,541	RUCO 4-5
Average	\$ 490,699	

Compare amounts from Company's response to RUCO 2-59a, Account 506100, Service Company Pension Charges:

Year	Capitalized	O&M	Total
2005	\$ 23,326	\$ 78,757	\$ 102,083
2006	\$ 100,747	\$ 1,624,692	\$ 1,725,439
2007	\$ 69,871	\$ 489,857	\$ 559,728
2008	\$ 46,979	\$ 495,909	\$ 542,888
Average 2006-2008		\$ 870,153	

Compare amounts from Company's response to RUCO 2-61, Account 506100, Pension:

Year	Amount
2005	\$ 96,878
2006	\$ 1,624,689 C
2007	\$ 489,857
2008	\$ 495,909
Average 2006-2008	\$ 870,152

C December 2005 had an unusually large charge due to the Company transition from ERISA to FAS 87 per RUCO 7-1:

2006 YTD November	\$ 320,510
2006 YTD November - annualized	\$ 349,647

Arizona American Water Company  
Management Fees - Normalize Affiliate OPEB Expense

Attachment RCS-6  
Schedule C-13  
Docket Nos. WSW-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water 9.3634% (A)	Sun City Water 12.2033% (B)	Anthem/ Agua Fria Wastewater 12.3543% (C)	Sun City Wastewater 7.5448% (D)	Sun City West Wastewater 6.3842% (E)	Total 47.8500% (F)	Reference
<b>Normalize Affiliate OPEB Expense in Management Fees:</b>								
1	Per AWWC	\$ 13,044	\$ 17,000	\$ 17,211	\$ 10,511	\$ 8,894	\$ 66,659	A
2	Per RUCO	\$ 11,634	\$ 15,163	\$ 15,350	\$ 9,374	\$ 7,932	\$ 59,454	B
3	Adjustment	\$ (1,410)	\$ (1,838)	\$ (1,860)	\$ (1,136)	\$ (961)	\$ (7,206)	
4	Subtotal Water						\$ (3,248)	
5	Subtotal Wastewater						\$ (3,958)	
6	Total Adjustment						\$ (7,206)	

Notes and Source

A Derived from Company's response to RUCO 4-3

Account	Description	Test Year Total Recorded	4% Pay Increase	Total Incentive Comp Removal
505100	PBOP	\$ 137,062	\$ 2,246	\$ 137,062

Compare amounts from Company's response to RUCO 4-5, Service Company Charges by Object Account (O&M):  
2008

505100	PBOP	\$ 137,062
--------	------	------------

B Reflects three-year average of 2006-2008 for a normalized allowance for affiliated OPEB expense

Year	Amount	Reference
2007	\$ 111,438	RUCO 4-5
2008	\$ 137,062	RUCO 4-5
Average	\$ 124,250	

Compare amounts from Company's response to RUCO 2-59a, Account 505100, Service Company OPEB Charges:

Year	Capitalized	O&M	Total
2005	\$ 29,024	\$ 116,116	\$ 145,140
2006	\$ 37,871	\$ 136,162	\$ 174,033
2007	\$ 15,890	\$ 111,438	\$ 127,328
2008	\$ 13,100	\$ 138,280	\$ 151,380
Average 2006-2008		\$ 128,627	\$ 128,627

Compare amounts from Company's response to RUCO 2-61, Account 505100, PBOP:

Year	Amount
2005	\$ 97,995
2006	\$ 136,162
2007	\$ 111,438
2008	\$ 138,280
Average 2006-2008	\$ 128,627

Test Year Ended December 31, 2008

Line No.	Description	Anthem Water 9.3634% (A)	Sun City Water 12.2033% (B)	Anthem/ Agua Fria Wastewater 12.3543% (C)	Sun City Wastewater 7.5448% (D)	Sun City West Wastewater 6.3842% (E)	Total 47.8500% (F)	Reference
<b>Remove Affiliate Charges for Business Development</b>								
1	Per AWWC	\$ 9,438	\$ 12,301	\$ 12,453	\$ 7,605	\$ 6,435	\$ 48,232	A
2	Per RUCO							B
3	Adjustment	\$ (9,438)	\$ (12,301)	\$ (12,453)	\$ (7,605)	\$ (6,435)	\$ (48,232)	
4	Subtotal Water						\$ (21,739)	
5	Subtotal Wastewater						\$ (26,493)	
6	Total Adjustment						\$ (48,232)	

Notes and Source

A Derived from Company's response to RUCO 4-3  
Total Business Development Expenses \$ 100,799

Compare: AAWC's response to RUCO 2-43(g):  
"Business development costs in the test year were \$101,395."

B Reflects removal of affiliate charges for business development



Arizona American Water Company  
Interest Synchronization

Attachment RCS-6  
Schedule C-15  
Docket No. W-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008  
(Thousands of Dollars)

Line No.	Description	Anthem Water (A)	Sun City Water (B)	Total Water (C)	Reference
1	Adjusted Rate Base, per RUCO	\$ 57,259,174	\$ 26,215,284	\$ 83,474,458	Schedules B (A) and B (SC)
2	Weighted Cost of Debt, per RUCO	3.05%	3.05%		Per RUCO - Schedule D
3	Deduction for Tax Purposes	\$ 1,748,695	\$ 800,615	\$ 2,549,310	L1 x L2
4	Interest Deduction per Company	\$ 1,722,960	\$ 845,582	\$ 2,568,542	Note A
5	Difference (Decreased) Increased Interest Deduction	\$ 25,735	\$ (44,967)	\$ (19,232)	L3 - L4
6	Combined Federal and State Income Tax Rates	38.60%	38.60%		
7	Increase (Decrease) to Income Tax	\$ (9,934)	\$ 17,357	\$ 7,423	L5 x L6

Notes and Source

A: AAWC Filing, Schedule C-1 (line 32) for each wastewater district referenced above

Arizona American Water Company  
 Depreciation Expense - Well 5.1 - Sun City Water

Test Year Ended December 31, 2008

Attachment RCS-6  
 Schedule C-16  
 Docket No. W-01303A-09-0343  
 Page 1 of 1

Line No.	Description	Sun City		Reference
		Water	(A)	
1	Remove Depreciation Expense Related to Post-Test Year Plant - Well 5.1	\$ (48,653)		A
2	Reverse Company Adjustment to Depreciation Expense Related to Old Well 5.1	\$ 11,692		A
3	Net Adjustment to Depreciation Expense	<u>\$ (36,961)</u>		

Notes and Source

A: Per Schedule B-2, Adjustment No. LJG-5 from AAWC filing

Test Year Ended December 31, 2008

Line No.	Account	Description	Amount (A)	Depreciation Rate* (B)	Depreciation Expense (C)	Reference
1	304300	Structures and Improvements - Water Treatment	\$ (22,289)	1.67%	\$ (372)	A
2	320100	Water Treatment Equipment - Non Media	\$ 22,289	7.06%	\$ 1,574	A
3		Net Adjustment to Depreciation Expense			<u>\$ 1,202</u>	

Notes and Source

A: These adjustments to depreciation expense reflect the impact of Staff's adjustment to reclassify the amount in Column A between the referenced accounts as discussed in the Rebuttal Testimony of Company witness Sandra L. Murrey

\* Depreciation rates from revised Company Adjustment SLM-1

**Arizona American Water Company**  
**Docket No. SW-01303A-09-0343**  
**Attachment RCS-7**  
**Accompanying the Surrebuttal Testimony of Ralph Smith**  
**RUCO Accounting Schedules - Wastewater Districts**

Number	Description	No. of Pages	Page No.	Note	Revised/ New
<b>Revenue Requirement Summary Schedules - Total Wastewater</b>					
A	Calculation of Revenue Deficiency (Sufficiency)	1	2		Revised
A-1	Gross Revenue Conversion Factor	1	3		Revised
B	Adjusted Rate Base	1	4		Revised
B.1	Summary of Rate Base Adjustments	1	5		Revised
C	Adjusted Net Operating Income	1	6		Revised
C.1	Summary of Net Operating Income Adjustments	3	7-9		Revised
D	Capital Structure and Cost Rates	1	10		
<b>Revenue Requirement Summary Schedules - Anthem/Agua Fria Wastewater</b>					
A (AAF)	Calculation of Revenue Deficiency (Sufficiency)	1	11		Revised
A-1(AAF)	Gross Revenue Conversion Factor	1	12		Revised
B(AAF)	Adjusted Rate Base	1	13		Revised
B.1(AAF)	Summary of Rate Base Adjustments	1	14		Revised
C(AAF)	Adjusted Net Operating Income	1	15		Revised
C.1(AAF)	Summary of Net Operating Income Adjustments	3	16-18		Revised
<b>Revenue Requirement Summary Schedules - Sun City Wastewater</b>					
A (SC)	Calculation of Revenue Deficiency (Sufficiency)	1	19		Revised
A-1(SC)	Gross Revenue Conversion Factor	1	20		Revised
B (SC)	Adjusted Rate Base	1	21		Revised
B.1 (SC)	Summary of Rate Base Adjustments	1	22		Revised
C (SC)	Adjusted Net Operating Income	1	23		Revised
C.1 (SC)	Summary of Net Operating Income Adjustments	2	24-25		Revised
<b>Revenue Requirement Summary Schedules - Sun City West Wastewater</b>					
A(SCW)	Calculation of Revenue Deficiency (Sufficiency)	1	26		Revised
A-1(SCW)	Gross Revenue Conversion Factor	1	27		Revised
B(SCW)	Adjusted Rate Base	1	28		Revised
B.1(SCW)	Summary of Rate Base Adjustments	1	29		Revised
C(SCW)	Adjusted Net Operating Income	1	30		Revised
C.1(SCW)	Summary of Net Operating Income Adjustments	3	31-33		Revised
<b>Rate Base Adjustments</b>					
B-2	Plant Retirements - Anthem/Agua Fria Wastewater	1	34		
B-3	Contributions In Aid of Construction			A	
B-4	Cash Working Capital	4	35-38		Revised
B-6	Verrado Wastewater Plant - Anthem/Agua Fria Wastewater	1	39		New
B-7	Comprehensive Planning Study	1	40		New
B-8	North West Valley Treatment Plant	1	41		New
B-9	Accumulated Deferred Income Taxes			A	New
<b>Net Operating Income Adjustments</b>					
C-2	Rate Case Expense	1	42		
C-3	Achievement Incentive Pay	1	43		
C-4	Stock-Based Compensation	1	44		Revised
C-5	Pension Expense	1	45		
C-5.1	Calculations for pension expense adjustment			A	
C-6	OPEB Expense	1	46		
C-7	Dues, Donations & Miscellaneous Expenses			A	
C-9	Management Fees - Other Expenses			A	
C-10	Management Fees - Remove AAWC's Requested Post Test Year Increase in Affiliate Employee Benefits			A	
C-11	Management Fees - Remove Affiliate Incentive Compensation Expense			A	
C-12	Management Fees - Normalize Affiliate Pension Expense			A	
C-13	Management Fees - Normalize Affiliate OPEB Expense			A	
C-14	Management Fees - Remove Business Development Expense			A	
C-15	Interest Synchronization	1	47		Revised
C-17	Depreciation Expense - Anthem/Agua Fria Wastewater	1	48		
C-19	Depreciation Expense - Anthem/Agua Fria Wastewater Reclassified Accounts	1	49		New
Total Pages (including Contents page)		49			

A: See Attachment RCS-6

Arizona American Water Company - Total of Wastewater Districts  
Calculation of Revenue Deficiency (Sufficiency)

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule A  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B	\$ 80,321,091	\$ 77,958,985	\$ (2,362,106)
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 6,851,421	\$ 5,280,942	\$ (1,570,479)
4	Adjusted net operating income	C	\$ 375,065	\$ 813,034	\$ 437,969
5	Net operating income deficiency		\$ 6,476,356	\$ 4,467,908	\$ (2,008,448)
6	Gross revenue conversion factor	A-1	1.6561	1.6561	
7	Revenue deficiency (Sufficiency)		\$ 10,725,216	\$ 7,399,124	\$ (3,326,092)

Percentage Increase Over Current Rates

8	Revenue from Sales to Retail Customers	Sch C, L.1	\$ 20,228,926	\$ 20,228,926	
9	Percentage Increase	L.7 / L.8	53.02%	36.58%	

Notes and Source

Col.A: AAWC Filing, Schedule A-1 (Anthem/Agua Fria, Sun City and Sun City West)

Calculation of RUCO recommended percentage increase to AAWC's base rates

AAWC's adjusted water revenues per Schedule C	RUCO Proposed
\$ 20,228,926	\$ 20,228,926
RUCO recommended rate increase (line 7 above)	\$ 7,399,124
Total revenues after reflecting RUCO recommended increase	\$ 27,628,050

Percentage change in revenues

36.58%

Calculation of AAWC's proposed percentage increase to base rates

AAWC's adjusted water revenues per Schedule C	AAWC Proposed
\$ 20,228,926	\$ 20,228,926
AAWC proposed rate increase (line 7 above)	\$ 10,725,216
Total revenues after reflecting AAWC proposed increase	\$ 30,954,142

Percentage change in revenues

53.02%

Arizona American Water Company - Anthem/Agua Fria Wastewater  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule A-1  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.71%	0.71%
3	Bad Debt Expense	0.31%	0.31%
4	Taxable Income as a Percent	98.98%	98.98%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.35%	67.35%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.38%	60.38%
9	<b>Gross Revenue Conversion Factor</b>	<b>1.6561</b>	<b>1.6561</b>

Notes and Source

Col.A:	AAWC Filing, Schedule C-3		
	Combined state and federal income tax rate	38.60%	38.60%

Components of Revenue Requirement Increase

	Amount	Percent
11 Net Income	\$ 4,467,916	60.38%
12 Federal Income Taxes	\$ 2,340,408	31.63%
13 State Income Taxes	\$ 515,571	6.97%
14 Property Taxes	\$ 52,269	0.71%
15 Uncollectibles	\$ 22,960	0.31%
16 Total Revenue Increase	\$ 7,399,124	100.00%
17 Total Revenue Increase (From Schedule A)	\$ 7,399,124	

Arizona American Water Company - Total of Wastewater Districts  
Adjusted Rate Base

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule B  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 191,762,219	\$ (1,891,273)	\$ 189,870,946
2	Accumulated Depreciation	\$ (52,782,874)	\$ 52,636	\$ (52,730,238)
3	<b>Net Utility Plant in Service</b>	<b>\$ 138,979,344</b>	<b>\$ (1,838,637)</b>	<b>\$ 137,140,707</b>
<b>Less:</b>				
4	Advances in Aid of Construction	\$ (51,079,109)	\$ -	\$ (51,079,109)
5	Contributions in Aid of Construction (net of amortization)	\$ (13,846,225)	\$ (69,233)	\$ (13,915,458)
6	Imputed Regulatory Advances	-	-	-
7	Imputed Regulatory Contributions	(947,395)	-	(947,395)
10	Deferred Income Taxes and Credits	4,117,012	(106,234)	4,010,778
11	Investment Tax Credits and Other Deferred Credits	-	-	-
12	<b>Total Reductions</b>	<b>\$ (61,755,717)</b>	<b>\$ (175,467)</b>	<b>\$ (61,931,184)</b>
<b>Plus:</b>				
13	Unamortized Finance Charges	-	-	-
14	Deferred Tax Assets	-	-	-
15	Deferred Debits	2,241,558	-	2,241,558
16	Allowance for Working Capital	855,905	(348,000)	507,905
17	Utility Plant Acquisition Adjustment	-	-	-
18	<b>Total Additions</b>	<b>\$ 3,097,462</b>	<b>\$ (348,000)</b>	<b>\$ 2,749,462</b>
19	<b>Total Rate Base</b>	<b>\$ 80,321,091</b>	<b>\$ (2,362,104)</b>	<b>\$ 77,958,985</b>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1

Arizona American Water Company - Total of Wastewater Districts  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule B.1  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments		Plant Retirements - Anthem/Agua Fria Wastewater		Contributions in Construction		Cash Working Capital		Verrado Wastewater Plant		Comprehensive Planning Study		Allocation of NWVTP		Accumulated Deferred Income Taxes				
				B-2	B-3	B-4	B-6	B-7	B-8	B-9	B-4	B-6	B-7	B-8	B-9	B-4	B-6	B-7	B-8	B-9
1	Gross Utility Plant in Service	\$	(1,891,273)	\$	(52,636)															
2	Accumulated Depreciation	\$	52,636	\$	52,636															
3	Net Utility Plant in Service	\$	(1,838,637)	\$	-	\$	-	\$	-	\$	(1,838,637)	\$	-	\$	-	\$	-	\$	-	\$
Less:																				
4	Advances in Aid of Construction	\$	-																	
5	Contributions in Aid of Construction (net of amortization)	\$	(69,233)	\$	(69,233)															
6	Imputed Regulatory Advances	\$	-																	
7	Imputed Regulatory Contributions	\$	-																	
10	Deferred Income Taxes and Credits	\$	(106,234)																	
11	Investment Tax Credits and Other Deferred Credits	\$	-																	
12	Total Reductions	\$	(175,467)	\$	(69,233)	\$	-	\$	-	\$	-	\$	-	\$	-	\$	-	\$	(106,234)	
Plus:																				
13	Unamortized Finance Charges	\$	-																	
14	Deferred Tax Assets	\$	-																	
15	Deferred Debits	\$	-																	
16	Allowance for Working Capital	\$	(348,000)																	
17	Utility Plant Acquisition Adjustment	\$	-																	
18	Total Additions	\$	(348,000)	\$	-	\$	-	\$	(348,000)	\$	-	\$	-	\$	-	\$	-	\$	-	\$
18	Total Rate Base	\$	(2,362,104)	\$	-	\$	(69,233)	\$	(348,000)	\$	(1,838,637)	\$	-	\$	-	\$	-	\$	(106,234)	

Notes and Source

See referenced exhibit for each adjustment



Arizona American Water Company - Total of Wastewater Districts  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule C  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Sewer Revenues	\$ 20,228,926	\$ -	\$ 20,228,926
2	Other Revenues	\$ 10,288	\$ -	\$ 10,288
3	<b>Total Revenues</b>	<u>\$ 20,239,214</u>	<u>\$ -</u>	<u>\$ 20,239,214</u>
<b>Operating Expenses</b>				
4	Labor	\$ 2,556,566	\$ (70,180)	\$ 2,486,386
5	Purchased Water	\$ 10,524	\$ -	\$ 10,524
6	Fuel & Power	\$ 679,980	\$ -	\$ 679,980
7	Chemicals	\$ 709,941	\$ -	\$ 709,941
8	Waste Disposal	\$ 3,602,842	\$ -	\$ 3,602,842
9	Management Fees	\$ 3,250,764	\$ (437,207)	\$ 2,813,557
10	Group Insurance	\$ 804,856	\$ (5,706)	\$ 799,150
11	Pensions	\$ 447,520	\$ (148,500)	\$ 299,020
12	Regulatory Expense	\$ 174,416	\$ (71,206)	\$ 103,210
13	Insurance Other Than Group	\$ 201,008	\$ -	\$ 201,008
14	Customer Accounting	\$ 511,824	\$ -	\$ 511,824
15	Rents	\$ 163,430	\$ -	\$ 163,430
16	General Office Expense	\$ 180,591	\$ -	\$ 180,591
17	Miscellaneous	\$ 882,166	\$ -	\$ 882,166
18	Maintenance Expense	\$ 446,357	\$ -	\$ 446,357
19	Depreciation & Amortization	\$ 5,749,606	\$ 1,414	\$ 5,751,020
20	General Taxes - Property Taxes	\$ 589,432	\$ -	\$ 589,432
21	General Taxes - Other	\$ 181,327	\$ -	\$ 181,327
22	Income Taxes	\$ (1,279,000)	\$ 293,419	\$ (985,581)
23	<b>Total Operating Expenses</b>	<u>\$ 19,864,150</u>	<u>\$ (437,966)</u>	<u>\$ 19,426,184</u>
24	<b>Utility Operating Income</b>	<u>\$ 375,064</u>	<u>\$ 437,966</u>	<u>\$ 813,030</u>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -	\$ -	\$ -
26	Interest Expense	\$ (2,409,633)	\$ -	\$ (2,409,633)
27	Other Expense	\$ (39,518)	\$ -	\$ (39,518)
28	Gain/Loss Sale of Fixed Assets	\$ 1	\$ -	\$ 1
29	<b>Total Other Additions/Deductions From Income</b>	<u>\$ (2,449,150)</u>	<u>\$ -</u>	<u>\$ (2,449,150)</u>
30	<b>Net Profit (Loss)</b>	<u>\$ (2,074,086)</u>	<u>\$ 437,966</u>	<u>\$ (1,636,120)</u>
31	Rate Base	<u>\$ 80,321,091</u>	<u>\$ (2,362,104)</u>	<u>\$ 77,958,987</u>
32	Earned Rate of Return	<u>0.47%</u>		<u>1.04%</u>

Notes and Source

Col.A: AAWC Filing, Schedule C-1  
Col.B: Schedule C.1  
Col.C: Col.A + Col.B

Arizona American Water Company - Total of Wastewater Districts  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-7  
Schedule C.1  
Docket No. SW-01303A-09-0343  
Page 1 of 3  
Revised

Attachment RCS-7  
Docket No. SW-01303A-09-0343  
Page 7 of 49

Line No.	Description	RUCO Adjustments	Rate Case Expense C-2	Achievement Incentive Pay C-3	Stock-Based Compensation C-4 Revised	Pension Expense C-5	OPEB Expense C-6
<b>Revenues</b>							
1	Sewer Revenues	\$ -					
2	Other Revenues	\$ -					
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Operating Expenses</b>							
4	Labor	\$ (70,180)		\$ (42,852)	\$ (27,328)		
5	Purchased Water	\$ -					
6	Fuel & Power	\$ -					
7	Chemicals	\$ -					
8	Waste Disposal	\$ -					
9	Management Fees	\$ (437,207)			\$ (18,286)		
10	Group Insurance	\$ (5,706)				\$ (5,706)	
11	Pensions	\$ (148,500)				\$ (148,500)	
12	Regulatory Expense	\$ (71,206)	\$ (71,206)				
13	Insurance Other Than Group	\$ -					
14	Customer Accounting	\$ -					
15	Rents	\$ -					
16	General Office Expense	\$ -					
17	Miscellaneous	\$ -					
18	Maintenance Expense	\$ -					
19	Depreciation & Amortization	\$ 1,414					
20	General Taxes - Property Taxes	\$ -					
21	General Taxes - Other	\$ -					
15	PRE-TAX OPERATING EXPENSES	\$ (731,385)	\$ (71,206)	\$ (42,852)	\$ (45,614)	\$ (148,500)	\$ (5,706)
16	PRE-TAX OPERATING INCOME	\$ 731,385	\$ 71,206	\$ 42,852	\$ 45,614	\$ 148,500	\$ 5,706
17	Income Taxes	\$ 293,419	\$ 27,486	\$ 16,541	\$ 17,607	\$ 57,321	\$ 2,203
18	TOTAL OPERATING EXPENSES	\$ (437,966)	\$ (43,720)	\$ (26,311)	\$ (28,007)	\$ (91,179)	\$ (3,503)
19	OPERATING INCOME	\$ 437,966	\$ 43,720	\$ 26,311	\$ 28,007	\$ 91,179	\$ 3,503

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3 38.60%

Attachment RCS-7  
Docket No. SW-01303A-09-0343  
Page 8 of 49

Notes and Source  
Combined Effective Tax Rate per AAWC filing, Schedule C-3

Arizona American Water Company - Total of Wastewater District  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Attachment RCS-7  
Schedule C.1  
Docket No. SW-01303A-09-0343  
Page 3 of 3  
Revised

Attachment RCS-7  
Docket No. SW-01303A-09-0343  
Page 9 of 49

Line No.	Description	Management Fees - Normalize Affiliate OPEB Expense C-13	Management Fees - Remove Business Development Expenses C-14	Interest Synchronization C-15 Revised	Depreciation Expense Related to Plant Retirements C-17	Depreciation Expense - Anthem/Agua Fria Wastewater Reclassified Accounts C-19 New
1	<b>Revenues</b>					
2	Sewer Revenues					
3	Other Revenues					
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -
	<b>Operating Expenses</b>					
4	Labor					
5	Purchased Water					
6	Fuel & Power					
7	Chemicals					
8	Waste Disposal					
9	Management Fees	\$ (3,958)	\$ (26,493)			
10	Group Insurance					
11	Pensions					
12	Regulatory Expense					
13	Insurance Other Than Group					
14	Customer Accounting					
15	Rents					
16	General Office Expense					
17	Miscellaneous					
18	Maintenance Expense					
19	Depreciation & Amortization					
20	General Taxes - Property Taxes					
21	General Taxes - Other					
15	PRE-TAX OPERATING EXPENSES	\$ (3,958)	\$ (26,493)	\$ -	\$ (2,853)	\$ 13,392
16	PRE-TAX OPERATING INCOME	\$ 3,958	\$ 26,493	\$ -	\$ 2,853	\$ (13,392)
17	Income Taxes	\$ 1,528	\$ 10,226	\$ 11,104	\$ 1,101	\$ (5,169)
18	TOTAL OPERATING EXPENSES	\$ (2,430)	\$ (16,267)	\$ 11,104	\$ (1,752)	\$ 8,223
19	OPERATING INCOME	\$ 2,430	\$ 16,267	\$ (11,104)	\$ 1,752	\$ (8,223)

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3

Arizona American Water Company - Wastewater Districts  
Capital Structure and Cost Rates

Attachment RCS-7  
Schedule D  
Docket No. SW-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Amount (A)	Percent (B)	Cost Rate (C)	Weighted Cost (D)
<b>Per Company</b>					
1	Long-Term Debt	\$ 188,208,140	54.85%	5.47%	3.00%
2	Short-Term Debt				
3	Stockholder's Equity	\$ 154,949,595	45.15%	12.25%	5.53%
4	Total	<u>\$ 343,157,735</u>	<u>100.00%</u>		<u>8.53%</u>
<b>Per RUCO</b>					
5	Long-Term Debt	\$ 188,208,140	47.56%	5.47%	2.60%
6	Short-Term Debt	\$ 52,584,000	13.29%	3.41%	0.45%
7	Stockholder's Equity	\$ 154,949,595	39.15%	9.50%	3.72%
8	Total	<u>\$ 395,741,735</u>	<u>100.00%</u>		<u>6.77%</u>
9	Difference				-1.756%
10	Weighted Cost of Debt				<u>3.05%</u>

Notes and Source

Lines 1-4: AAWC Filing, Schedule D-1 (reflects end of projected test year capital structure)

Lines 5-8: Per RUCO witness William Rigsby (reflects end of test year capital structure)

Arizona American Water Company - Anthem/Agua Fria Wastewater  
Calculation of Revenue Deficiency (Sufficiency)

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule A (AAF)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B (AAF)	\$ 47,735,732	\$ 45,264,942	\$ (2,470,790)
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 4,071,858	\$ 3,066,247	\$ (1,005,611)
4	Adjusted net operating income	C (AAF)	\$ (191,785)	\$ (4,298)	\$ 187,487
5	Net operating income deficiency		\$ 4,263,643	\$ 3,070,545	\$ (1,193,098)
6	Gross revenue conversion factor	A-1 (AAF)	1.6561	1.6561	
7	Revenue deficiency (Sufficiency)		\$ 7,060,837	\$ 5,085,007	\$ (1,975,830)

Percentage Increase Over Current Rates

8	Revenue from Sales to Retail Customers	Sch C (AAF), L.1	\$ 8,634,567	\$ 8,634,567	
9	Percentage Increase	L.7 / L.8	81.77%	58.89%	

Notes and Source

Col.A: AAWC Filing, Schedule A-1

Calculation of RUCO recommended percentage increase to AAWC's base rates

AAWC's adjusted water revenues per Schedule C (AAF)	RUCO Proposed
RUCO recommended rate increase (line 7 above)	\$ 8,634,567
Total revenues after reflecting RUCO recommended increase	\$ 5,085,007
Percentage change in revenues	\$ 13,719,574
	58.89%

Calculation of AAWC's proposed percentage increase to base rates

AAWC's adjusted water revenues per Schedule C (AAF)	AAWC Proposed
AAWC proposed rate increase (line 7 above)	\$ 8,634,567
Total revenues after reflecting AAWC proposed increase	\$ 7,060,837
Percentage change in revenues	\$ 15,695,404
	81.77%

Arizona American Water Company - Anthem/Agua Fria Wastewater  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule A-1 (AAF)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.71%	0.71%
3	Bad Debt Expense	0.31%	0.31%
4	Taxable Income as a Percent	98.98%	98.98%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.35%	67.35%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.38%	60.38%
9	<b>Gross Revenue Conversion Factor</b>	<b>1.6561</b>	<b>1.6561</b>

Notes and Source

Col.A: AAWC Filing, Schedule C-3

Combined state and federal income tax rate	38.60%	38.60%
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**Components of Revenue Requirement Increase**

	Amount	Percent
11 Net Income	\$ 3,070,551	60.38%
12 Federal Income Taxes	\$ 1,608,432	31.63%
13 State Income Taxes	\$ 354,323	6.97%
14 Property Taxes	\$ 35,922	0.71%
15 Uncollectibles	\$ 15,779	0.31%
16 Total Revenue Increase	<u>\$ 5,085,007</u>	<u>100.00%</u>
17 Total Revenue Increase (From Schedule A (AAF))	<u>\$ 5,085,007</u>	

Arizona American Water Company - Anthem/Agua Fria Wastewater  
Adjusted Rate Base

Attachment RCS-7  
Schedule B (AAF)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 131,361,186	\$ (2,931,096)	\$ 128,430,090
2	Accumulated Depreciation	\$ (22,837,366)	\$ 682,880	\$ (22,154,486)
3	<b>Net Utility Plant in Service</b>	<b>\$ 108,523,819</b>	<b>\$ (2,248,216)</b>	<b>\$ 106,275,603</b>
<b>Less:</b>				
4	Advances in Aid of Construction	\$ (48,273,364)	\$ -	\$ (48,273,364)
5	Contributions in Aid of Construction (net of amortization)	\$ (13,829,151)	\$ (65,490)	\$ (13,894,641)
6	Imputed Regulatory Advances	\$ -	\$ -	\$ -
7	Imputed Regulatory Contributions	\$ (143,475)	\$ -	\$ (143,475)
10	Deferred Income Taxes and Credits	\$ 1,049,621	\$ (27,084)	\$ 1,022,537
11	Investment Tax Credits and Other Deferred Credits	\$ -	\$ -	\$ -
12	<b>Total Reductions</b>	<b>\$ (61,196,369)</b>	<b>\$ (92,574)</b>	<b>\$ (61,288,943)</b>
<b>Plus:</b>				
13	Unamortized Finance Charges	\$ -	\$ -	\$ -
14	Deferred Tax Assets	\$ -	\$ -	\$ -
15	Deferred Debits	\$ 75,382	\$ -	\$ 75,382
16	Allowance for Working Capital	\$ 332,901	\$ (130,000)	\$ 202,901
17	Utility Plant Acquisition Adjustment	\$ -	\$ -	\$ -
18	<b>Total Additions</b>	<b>\$ 408,282</b>	<b>\$ (130,000)</b>	<b>\$ 278,282</b>
19	<b>Total Rate Base</b>	<b>\$ 47,735,732</b>	<b>\$ (2,470,790)</b>	<b>\$ 45,264,942</b>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1



Arizona American Water Company - Anthem/Agua Fria Wastewater  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule B.1 (AAF)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments	Plant Retirements - Anthem/Agua Fria Wastewater B-2	Contributions in Aid of Construction B-3	Cash Working Capital B-4 Revised	Verrado Wastewater Plant B-6 New	Allocation of NW/TP B-8 New	Accumulated Deferred Income Taxes B-9 New
1	Gross Utility Plant in Service	\$ (2,931,096)	\$ (52,636)			\$ (1,838,637)	\$ (1,039,823)	
2	Accumulated Depreciation	\$ 682,880	\$ 52,636				\$ 630,244	
3	<b>Net Utility Plant in Service</b>	<b>\$ (2,248,216)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (1,838,637)</b>	<b>\$ (409,579)</b>	<b>\$ -</b>
<b>Less:</b>								
4	Advances in Aid of Construction	\$ -						
5	Contributions in Aid of Construction (net of amortization)	\$ (65,490)		\$ (65,490)				
6	Imputed Regulatory Advances	\$ -						
7	Imputed Regulatory Contributions	\$ -						
10	Deferred Income Taxes and Credits	\$ (27,084)						\$ (27,084)
11	Investment Tax Credits and Other Deferred Credits	\$ -						
12	<b>Total Reductions</b>	<b>\$ (92,574)</b>	<b>\$ -</b>	<b>\$ (65,490)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (27,084)</b>
<b>Plus:</b>								
13	Unamortized Finance Charges	\$ -						
14	Deferred Tax Assets	\$ -						
15	Deferred Debits	\$ -						
16	Allowance for Working Capital	\$ (130,000)			\$ (130,000)			
17	Utility Plant Acquisition Adjustment	\$ -						
18	<b>Total Additions</b>	<b>\$ (130,000)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (130,000)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>
18	<b>Total Rate Base</b>	<b>\$ (2,470,790)</b>	<b>\$ -</b>	<b>\$ (65,490)</b>	<b>\$ (130,000)</b>	<b>\$ (1,838,637)</b>	<b>\$ (409,579)</b>	<b>\$ (27,084)</b>

Notes and Source  
See referenced exhibit for each adjustment

Arizona American Water Company - Anthem/Agua Fria Wastewater  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule C (AAF)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Sewer Revenues	\$ 8,634,567	\$ -	\$ 8,634,567
2	Other Revenues	\$ 2,556	\$ -	\$ 2,556
3	<b>Total Revenues</b>	<u>\$ 8,637,123</u>	<u>\$ -</u>	<u>\$ 8,637,123</u>
<b>Operating Expenses</b>				
4	Labor	\$ 1,335,278	\$ (30,484)	\$ 1,304,794
5	Purchased Water	\$ 3,368	\$ -	\$ 3,368
6	Fuel & Power	\$ 278,664	\$ -	\$ 278,664
7	Chemicals	\$ 303,374	\$ -	\$ 303,374
8	Waste Disposal	\$ 199,095	\$ -	\$ 199,095
9	Management Fees	\$ 1,528,005	\$ (205,507)	\$ 1,322,498
10	Group Insurance	\$ 396,599	\$ (2,682)	\$ 393,917
11	Pensions	\$ 221,640	\$ (72,483)	\$ 149,157
12	Regulatory Expense	\$ 80,939	\$ (31,679)	\$ 49,260
13	Insurance Other Than Group	\$ 94,566	\$ -	\$ 94,566
14	Customer Accounting	\$ 242,170	\$ -	\$ 242,170
15	Rents	\$ 84,483	\$ -	\$ 84,483
16	General Office Expense	\$ 85,697	\$ -	\$ 85,697
17	Miscellaneous	\$ 534,489	\$ (4,289)	\$ 530,200
18	Maintenance Expense	\$ 246,204	\$ -	\$ 246,204
19	Depreciation & Amortization	\$ 3,830,808	\$ 10,539	\$ 3,841,347
20	General Taxes - Property Taxes	\$ 296,804	\$ -	\$ 296,804
21	General Taxes - Other	\$ 87,538	\$ -	\$ 87,538
22	Income Taxes	\$ (1,020,813)	\$ 149,098	\$ (871,715)
23	<b>Total Operating Expenses</b>	<u>\$ 8,828,908</u>	<u>\$ (187,487)</u>	<u>\$ 8,641,421</u>
24	<b>Utility Operating Income</b>	<u>\$ (191,785)</u>	<u>\$ 187,487</u>	<u>\$ (4,298)</u>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -		\$ -
26	Interest Expense	\$ (1,432,072)		\$ (1,432,072)
27	Other Expense	\$ (18,575)		\$ (18,575)
28	Gain/Loss Sale of Fixed Assets	\$ (4)		\$ (4)
29	<b>Total Other Additions/Deductions From Income</b>	<u>\$ (1,450,651)</u>	<u>\$ -</u>	<u>\$ (1,450,651)</u>
30	<b>Net Profit (Loss)</b>	<u>\$ (1,642,436)</u>	<u>\$ 187,487</u>	<u>\$ (1,454,949)</u>
31	Rate Base	<u>\$ 47,735,732</u>	<u>\$ (2,470,790)</u>	<u>\$ 45,264,942</u>
32	Earned Rate of Return	<u>-0.40%</u>		<u>-0.01%</u>

Notes and Source

Col.A: AAWC Filing, Schedule C-1

Col.B: Schedule C.1

Col.C: Col.A + Col.B

Arizona American Water Company - Anthem/Agua Fria Wastewater  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	RUCO Adjustments	Rate Case Expense C-2	Achievement Incentive Pay C-3	Stock-Based Compensation C-4 Revised	Pension Expense C-5	OPEB Expense C-6
<b>Revenues</b>							
1	Sewer Revenues	\$ -					
2	Other Revenues	\$ -					
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Operating Expenses</b>							
4	Labor	\$ (30,484)		\$ (17,639)	\$ (12,845)		
5	Purchased Water	\$ -					
6	Fuel & Power	\$ -					
7	Chemicals	\$ -					
8	Waste Disposal	\$ -					
9	Management Fees	\$ (205,507)			\$ (8,595)		
10	Group Insurance	\$ (2,682)					
11	Pensions	\$ (72,483)				\$ (72,483)	\$ (2,682)
12	Regulatory Expense	\$ (31,679)	\$ (31,679)				
13	Insurance Other Than Group	\$ -					
14	Customer Accounting	\$ -					
15	Rents	\$ -					
16	General Office Expense	\$ -					
17	Miscellaneous	\$ (4,289)					
18	Maintenance Expense	\$ -					
19	Depreciation & Amortization	\$ 10,539					
20	General Taxes - Property Taxes	\$ -					
21	General Taxes - Other	\$ -					
15	<b>PRE-TAX OPERATING EXPENSES</b>	\$ (336,585)	\$ (31,679)	\$ (17,639)	\$ (21,440)	\$ (72,483)	\$ (2,682)
16	<b>PRE-TAX OPERATING INCOME</b>	\$ 336,585	\$ 31,679	\$ 17,639	\$ 21,440	\$ 72,483	\$ 2,682
17	Income Taxes	\$ 149,098	\$ 12,228	\$ 6,809	\$ 8,276	\$ 27,978	\$ 1,035
18	<b>TOTAL OPERATING EXPENSES</b>	\$ (187,487)	\$ (19,451)	\$ (10,830)	\$ (13,164)	\$ (44,505)	\$ (1,647)
19	<b>OPERATING INCOME</b>	\$ 187,487	\$ 19,451	\$ 10,830	\$ 13,164	\$ 44,505	\$ 1,647

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3

38.60%

Arizona American Water Company - Anthem/Agua Fria Wastew  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	Dues, Donations & Misc. Expenses C-7	Management Fees - 4% Post-Test Year Increase C-9A	Management Fees - Affiliate Employee Benefits C-10	Management Fees - Affiliate Incentive Compensation C-11	Management Fees - Normalize Affiliate Pension Expense C-12
			New			
	<b>Revenues</b>					
1	Sewer Revenues					
2	Other Revenues					
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -
	<b>Operating Expenses</b>					
4	Labor					
5	Purchased Water					
6	Fuel & Power					
7	Chemicals					
8	Waste Disposal					
9	Management Fees					
10	Group Insurance					
11	Pensions					
12	Regulatory Expense					
13	Insurance Other Than Group					
14	Customer Accounting					
15	Rents					
16	General Office Expense					
17	Miscellaneous					
18	Maintenance Expense					
19	Depreciation & Amortization					
20	General Taxes - Property Taxes					
21	General Taxes - Other					
15	PRE-TAX OPERATING EXPENSES	\$ (4,289)	\$ (21,050)	\$ (23,154)	\$ (70,978)	\$ (66,317)
16	PRE-TAX OPERATING INCOME	\$ 4,289	\$ 21,050	\$ 23,154	\$ 70,978	\$ 66,317
17	Income Taxes	\$ 1,656	\$ 8,125	\$ 8,937	\$ 27,398	\$ 25,598
18	TOTAL OPERATING EXPENSES	\$ (2,633)	\$ (12,925)	\$ (14,217)	\$ (43,580)	\$ (40,719)
19	OPERATING INCOME	\$ 2,633	\$ 12,925	\$ 14,217	\$ 43,580	\$ 40,719

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3

Arizona American Water Company - Anthem/Agua Fria Wastew  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	Management Fees - Normalize Affiliate OPEB Expense C-13	Management Fees - Remove Business Development Expenses C-14	Interest Synchronization C-15 Revised	Depreciation Expense - Related to Plant Retirements C-17	Depreciation Expense - Anthem/Agua Fria Wastewater Reclassified Accounts C-19 New
1	<b>Revenues</b>					
2	Sewer Revenues					
3	Other Revenues					
	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -
4	<b>Operating Expenses</b>					
5	Labor					
6	Purchased Water					
7	Fuel & Power					
8	Chemicals					
9	Waste Disposal					
10	Management Fees	\$ (1,860)	\$ (12,453)			
11	Group Insurance					
12	Pensions					
13	Regulatory Expense					
14	Insurance Other Than Group					
15	Customer Accounting					
16	Rents					
17	General Office Expense					
18	Miscellaneous					
19	Maintenance Expense					
20	Depreciation & Amortization					
21	General Taxes - Property Taxes					
22	General Taxes - Other					
23	PRE-TAX OPERATING EXPENSES	\$ (1,860)	\$ (12,453)	\$ -	\$ (2,853)	\$ 13,392
24	PRE-TAX OPERATING INCOME	\$ 1,860	\$ 12,453	\$ -	\$ 2,853	\$ (13,392)
25	Income Taxes	\$ 718	\$ 4,807	\$ 19,177	\$ 1,101	\$ (5,169)
26	TOTAL OPERATING EXPENSES	\$ (1,142)	\$ (7,646)	\$ 19,177	\$ (1,752)	\$ 8,223
27	OPERATING INCOME	\$ 1,142	\$ 7,646	\$ (19,177)	\$ 1,752	\$ (8,223)

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3

Arizona American Water Company - Sun City Wastewater  
Calculation of Revenue Deficiency (Sufficiency)

Attachment RCS-7  
Schedule A (SC)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B (SC)	\$ 14,764,087	\$ 14,596,027	\$ (168,060)
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 1,259,377	\$ 988,735	\$ (270,642)
4	Adjusted net operating income	C (SC)	\$ (51,593)	\$ 68,704	\$ 120,297
5	Net operating income deficiency		\$ 1,310,969	\$ 920,031	\$ (390,938)
6	Gross revenue conversion factor	A-1 (SC)	1.6453	1.6453	
7	Revenue deficiency (Sufficiency)		\$ 2,156,882	\$ 1,513,691	\$ (643,191)

Percentage Increase Over Current Rates

8	Revenue from Sales to Retail Customers	Sch C (SC), L.1	\$ 5,933,970	\$ 5,933,970	
9	Percentage Increase	L.7 / L.8	36.35%	25.51%	

Notes and Source

Col.A: AAWC Filing, Schedule A-1

Calculation of RUCO recommended percentage increase to AAWC's base rates

AAWC's adjusted water revenues per Schedule C (SC)	RUCO Proposed
RUCO recommended rate increase (line 7 above)	\$ 5,933,970
Total revenues after reflecting RUCO recommended increase	\$ 1,513,691
	\$ 7,447,661
Percentage change in revenues	25.51%

Calculation of AAWC's proposed percentage increase to base rates

AAWC's adjusted water revenues per Schedule C (SC)	AAWC Proposed
AAWC proposed rate increase (line 7 above)	\$ 5,933,970
Total revenues after reflecting AAWC proposed increase	\$ 2,156,882
Percentage change in revenues	\$ 8,090,852
	36.35%

Arizona American Water Company - Sun City Wastewater  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule A-1 (SC)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.54%	0.54%
3	Bad Debt Expense	0.08%	0.08%
4	Taxable Income as a Percent	99.38%	99.38%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.75%	67.75%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.78%	60.78%
9	<b>Gross Revenue Conversion Factor</b>	<b>1.6453</b>	<b>1.6453</b>

Notes and Source

Col.A:	AAWC Filing, Schedule C-3		
	Combined state and federal income tax rate	38.60%	38.60%

Components of Revenue Requirement Increase

	Amount	Percent
11 Net Income	\$ 920,033	60.78%
12 Federal Income Taxes	\$ 478,794	31.63%
13 State Income Taxes	\$ 105,474	6.97%
14 Property Taxes	\$ 8,208	0.54%
15 Uncollectibles	\$ 1,182	0.08%
16 Total Revenue Increase	\$ 1,513,691	100.00%
17 Total Revenue Increase (From Schedule A (SC))	\$ 1,513,691	

Arizona American Water Company - Sun City Wastewater  
Adjusted Rate Base

Attachment RCS-7  
Schedule B (SC)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 24,469,337	\$ (12,242)	\$ 24,457,095
2	Accumulated Depreciation	\$ (10,761,769)	\$ -	\$ (10,761,769)
3	<b>Net Utility Plant in Service</b>	<u>\$ 13,707,569</u>	<u>\$ (12,242)</u>	<u>\$ 13,695,327</u>
<b>Less:</b>				
4	Advances in Aid of Construction	\$ (2,660,292)	\$ -	\$ (2,660,292)
5	Contributions in Aid of Construction (net of amortization)	\$ (12,327)	\$ (3,743)	\$ (16,070)
6	Imputed Regulatory Advances	\$ -	\$ -	\$ -
7	Imputed Regulatory Contributions	\$ (360,708)	\$ -	\$ (360,708)
10	Deferred Income Taxes and Credits	\$ 1,824,256	\$ (47,073)	\$ 1,777,183
11	Investment Tax Credits and Other Deferred Credits	\$ -	\$ -	\$ -
12	<b>Total Reductions</b>	<u>\$ (1,209,071)</u>	<u>\$ (50,816)</u>	<u>\$ (1,259,887)</u>
<b>Plus:</b>				
13	Unamortized Finance Charges	\$ -	\$ -	\$ -
14	Deferred Tax Assets	\$ -	\$ -	\$ -
15	Deferred Debits	\$ 2,057,405	\$ -	\$ 2,057,405
16	Allowance for Working Capital	\$ 208,182	\$ (105,000)	\$ 103,182
17	Utility Plant Acquisition Adjustment	\$ -	\$ -	\$ -
18	<b>Total Additions</b>	<u>\$ 2,265,587</u>	<u>\$ (105,000)</u>	<u>\$ 2,160,587</u>
19	<b>Total Rate Base</b>	<u>\$ 14,764,087</u>	<u>\$ (168,058)</u>	<u>\$ 14,596,027</u>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1



Arizona American Water Company - Sun City Wastewater  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule B.1 (SC)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments	Contributions in Aid of Construction B-3	Cash Working Capital B-4 Revised	Comprehensive Planning Study B-7 New	Accumulated Deferred Income Taxes B-9 New
1	Gross Utility Plant in Service	\$ (12,242)			\$ (12,242)	
2	Accumulated Depreciation	\$ -				
3	<b>Net Utility Plant in Service</b>	<u>\$ (12,242)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (12,242)</u>	<u>\$ -</u>
<b>Less:</b>						
4	Advances in Aid of Construction	\$ -				
5	Contributions in Aid of Construction (net of amortization)	\$ (3,743)	\$ (3,743)			
6	Imputed Regulatory Advances	\$ -				
7	Imputed Regulatory Contributions	\$ -				
10	Deferred Income Taxes and Credits	\$ (47,073)				\$ (47,073)
11	Investment Tax Credits and Other Deferred Credits	\$ -				
12	<b>Total Reductions</b>	<u>\$ (50,816)</u>	<u>\$ (3,743)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (47,073)</u>
<b>Plus:</b>						
13	Unamortized Finance Charges,	\$ -				
14	Deferred Tax Assets	\$ -				
15	Deferred Debits	\$ -				
16	Allowance for Working Capital	\$ (105,000)		\$ (105,000)		
17	Utility Plant Acquisition Adjustment	\$ -				
18	<b>Total Additions</b>	<u>\$ (105,000)</u>	<u>\$ -</u>	<u>\$ (105,000)</u>	<u>\$ -</u>	<u>\$ -</u>
18	<b>Total Rate Base</b>	<u>\$ (168,058)</u>	<u>\$ (3,743)</u>	<u>\$ (105,000)</u>	<u>\$ (12,242)</u>	<u>\$ (47,073)</u>

Notes and Source

See referenced exhibit for each adjustment

Arizona American Water Company - Sun City Wastewater  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule C (SC)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Sewer Revenues	\$ 5,933,970	\$ -	\$ 5,933,970
2	Other Revenues	\$ 6,411	\$ -	\$ 6,411
3	<b>Total Revenues</b>	<b>\$ 5,940,381</b>	<b>\$ -</b>	<b>\$ 5,940,381</b>
<b>Operating Expenses</b>				
4	Labor	\$ 454,529	\$ (18,617)	\$ 435,912
5	Purchased Water	\$ -	\$ -	\$ -
6	Fuel & Power	\$ 15,804	\$ -	\$ 15,804
7	Chemicals	\$ 4,885	\$ -	\$ 4,885
8	Waste Disposal	\$ 3,300,475	\$ -	\$ 3,300,475
9	Management Fees	\$ 933,155	\$ (125,503)	\$ 807,652
10	Group Insurance	\$ 141,193	\$ (1,638)	\$ 139,555
11	Pensions	\$ 75,595	\$ (25,187)	\$ 50,408
12	Regulatory Expense	\$ 49,683	\$ (20,573)	\$ 29,110
13	Insurance Other Than Group	\$ 57,656	\$ -	\$ 57,656
14	Customer Accounting	\$ 145,686	\$ -	\$ 145,686
15	Rents	\$ 40,868	\$ -	\$ 40,868
16	General Office Expense	\$ 44,944	\$ -	\$ 44,944
17	Miscellaneous	\$ 104,503	\$ (2,620)	\$ 101,883
18	Maintenance Expense	\$ 61,533	\$ -	\$ 61,533
19	Depreciation & Amortization	\$ 679,999	\$ -	\$ 679,999
20	General Taxes - Property Taxes	\$ 157,456	\$ -	\$ 157,456
21	General Taxes - Other	\$ 34,880	\$ -	\$ 34,880
22	Income Taxes	\$ (310,869)	\$ 73,841	\$ (237,028)
23	<b>Total Operating Expenses</b>	<b>\$ 5,991,974</b>	<b>\$ (120,297)</b>	<b>\$ 5,871,677</b>
24	<b>Utility Operating Income</b>	<b>\$ (51,593)</b>	<b>\$ 120,297</b>	<b>\$ 68,704</b>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -		\$ -
26	Interest Expense	\$ (442,923)		\$ (442,923)
27	Other Expense	\$ (11,344)		\$ (11,344)
28	Gain/Loss Sale of Fixed Assets	\$ 3		\$ 3
29	<b>Total Other Additions/Deductions From Income</b>	<b>\$ (454,264)</b>	<b>\$ -</b>	<b>\$ (454,264)</b>
30	<b>Net Profit (Loss)</b>	<b>\$ (505,857)</b>	<b>\$ 120,297</b>	<b>\$ (385,560)</b>
31	Rate Base	\$ 14,764,087	\$ (168,058)	\$ 14,596,029
32	Earned Rate of Return	-0.35%		0.47%

Notes and Source

Col.A: AAWC Filing, Schedule C-1

Col.B: Schedule C.1

Col.C: Col.A + Col.B

Arizona American Water Company - Sun City Wastewater  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	RUCO Adjustments	Rate Case Expense C-2	Achievement Incentive Pay C-3	Stock-Based Compensation C-4	Pension Expense C-5	OPEB Expense C-6	Dues, Donations & Miscellaneous Expenses C-7
<b>Revenues</b>								
1	Sewer Revenues	\$ -						
2	Other Revenues	\$ -						
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Operating Expenses</b>								
4	Labor	\$ (18,617)		\$ (10,772)	\$ (7,845)			
5	Purchased Water	\$ -						
6	Fuel & Power	\$ -						
7	Chemicals	\$ -						
8	Waste Disposal	\$ -						
9	Management Fees	\$ (125,503)			\$ (5,249)			
10	Group Insurance	\$ (1,638)						
11	Pensions	\$ (25,187)				\$ (25,187)		\$ (1,638)
12	Regulatory Expense	\$ (20,573)	\$ (20,573)					
13	Insurance Other Than Group	\$ -						
14	Customer Accounting	\$ -						
15	Rents	\$ -						
16	General Office Expense	\$ -						
17	Miscellaneous	\$ (2,620)						\$ (2,620)
18	Maintenance Expense	\$ -						
19	Depreciation & Amortization	\$ -						
20	General Taxes - Property Taxes	\$ -						
21	General Taxes - Other	\$ -						
15	PRE-TAX OPERATING EXPENSES	\$ (194,138)	\$ (20,573)	\$ (10,772)	\$ (13,094)	\$ (25,187)	\$ (1,638)	\$ (2,620)
16	PRE-TAX OPERATING INCOME	\$ 194,138	\$ 20,573	\$ 10,772	\$ 13,094	\$ 25,187	\$ 1,638	\$ 2,620
17	Income Taxes	\$ 73,841	\$ 7,941	\$ 4,158	\$ 5,054	\$ 9,722	\$ 632	\$ 1,011
18	TOTAL OPERATING EXPENSES	\$ (120,297)	\$ (12,632)	\$ (6,614)	\$ (8,040)	\$ (15,465)	\$ (1,006)	\$ (1,609)
19	OPERATING INCOME	\$ 120,297	\$ 12,632	\$ 6,614	\$ 8,040	\$ 15,465	\$ 1,006	\$ 1,609

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3 38.60%

Arizona American Water Company - Sun City Wastew  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	Management Fees - Other Expenses C-9	Management Fees - 4% Post-Test Year Wage Increase C-9A	Management Fees - Employee Benefits C-10	Management Fees - Affiliate Incentive Compensation C-11	Management Fees - Normalize Affiliate Pension Expense C-12	Management Fees - Normalize Affiliate OPEB Expense C-13	Management Fees - Remove Business Development Expenses C-14	Interest Synchronization C-15	Revised
1	Revenues									
2	Sewer Revenues									
3	Other Revenues									
	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
4	Operating Expenses									
5	Labor									
6	Purchased Water									
7	Fuel & Power									
8	Chemicals									
9	Waste Disposal									
10	Management Fees	\$ (12,855)	\$ (14,140)	\$ (43,347)	\$ (40,500)	\$ (671)	\$ (1,136)	\$ (7,605)		
11	Group Insurance									
12	Pensions									
13	Regulatory Expense									
14	Insurance Other Than Group									
15	Customer Accounting									
16	Rents									
17	General Office Expense									
18	Miscellaneous									
19	Maintenance Expense									
20	Depreciation & Amortization									
21	General Taxes - Property Taxes									
15	General Taxes - Other									
15	PRE-TAX OPERATING EXPENSES	\$ (12,855)	\$ (14,140)	\$ (43,347)	\$ (40,500)	\$ (671)	\$ (1,136)	\$ (7,605)	\$ -	\$ -
16	PRE-TAX OPERATING INCOME	\$ 12,855	\$ 14,140	\$ 43,347	\$ 40,500	\$ 671	\$ 1,136	\$ 7,605	\$ -	\$ -
17	Income Taxes	\$ 4,962	\$ 5,458	\$ 16,732	\$ 15,633	\$ 259	\$ 439	\$ 2,936	\$ (1,096)	\$ (1,096)
18	TOTAL OPERATING EXPENSES	\$ (7,893)	\$ (8,682)	\$ (26,615)	\$ (24,867)	\$ (412)	\$ (697)	\$ (4,669)	\$ (1,096)	\$ (1,096)
19	OPERATING INCOME	\$ 7,893	\$ 8,682	\$ 26,615	\$ 24,867	\$ 412	\$ 697	\$ 4,669	\$ 1,096	\$ 1,096

Notes and Source  
Combined Effective Tax Rate per AAWC filing, Schedi

Arizona American Water Company - Sun City West Wastewater  
Calculation of Revenue Deficiency (Sufficiency)

Attachment RCS-7  
Schedule A (SCW)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Reference	Per Company (A)	Per RUCO (B)	Difference (C)
1	Adjusted rate base	B (SCW)	\$ 17,821,272	\$ 18,098,016	\$ 276,744
2	Rate of return	D	8.53%	6.77%	
3	Net operating income required		\$ 1,520,155	\$ 1,225,960	\$ (294,195)
4	Adjusted net operating income	C (SCW)	\$ 618,443	\$ 748,629	\$ 130,186
5	Net operating income deficiency		\$ 901,712	\$ 477,331	\$ (424,381)
6	Gross revenue conversion factor	A-1 (SCW)	1.6422	1.6422	
7	Revenue deficiency (Sufficiency)		\$ 1,480,756	\$ 783,855	\$ (696,901)
Percentage Increase Over Current Rates					
8	Revenue from Sales to Retail Customers	Sch C (SCW), L.1	\$ 5,660,389	\$ 5,660,389	
9	Percentage Increase	L.7 / L.8	26.16%	13.85%	

Notes and Source

Col.A: AAWC Filing, Revised Schedule A-1

Calculation of RUCO recommended percentage increase to AAWC's base rates

AAWC's adjusted water revenues per Schedule C (SCW)	RUCO Proposed
RUCO recommended rate increase (line 7 above)	\$ 5,660,389
Total revenues after reflecting RUCO recommended increase	\$ 783,855
	\$ 6,444,244
Percentage change in revenues	13.85%

Calculation of AAWC's proposed percentage increase to base rates

AAWC's adjusted water revenues per Schedule C (SCW)	AAWC Proposed
AAWC proposed rate increase (line 7 above)	\$ 5,660,389
Total revenues after reflecting AAWC proposed increase	\$ 1,480,756
	\$ 7,141,145
Percentage change in revenues	26.16%

Arizona American Water Company - Sun City West Wastewater  
Gross Revenue Conversion Factor

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule A-1 (SCW)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Company Proposed (A)	RUCO Proposed (B)
1	Gross Revenue	100.00%	100.00%
	Less:		
2	Property Taxes	0.49%	0.49%
3	Bad Debt Expense	0.02%	0.02%
4	Taxable Income as a Percent	99.49%	99.49%
5	Less: Federal Income Taxes	31.63%	31.63%
6	Taxable Income as a Percent	67.86%	67.86%
7	Less: State Income Taxes	6.97%	6.97%
8	Change in Net Operating Income	60.90%	60.90%
9	Gross Revenue Conversion Factor	1.6422	1.6422

Notes and Source

Col.A: AAWC Filing, Schedule C-3		
Combined state and federal income tax rate	38.60%	38.60%

Components of Revenue Requirement Increase

	Amount	Percent
11 Net Income	\$ 477,331	60.90%
12 Federal Income Taxes	\$ 247,940	31.63%
13 State Income Taxes	\$ 54,619	6.97%
14 Property Taxes	\$ 3,828	0.49%
15 Uncollectibles	\$ 136	0.02%
16 Total Revenue Increase	\$ 783,854	100.00%
17 Total Revenue Increase (From Schedule A (SCW))	\$ 783,855	

Arizona American Water Company - Sun City West Wastewater  
Adjusted Rate Base

Attachment RCS-7  
Schedule B (SCW)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Test Year Ended December 31, 2008

Line No.	Description	Company Proposed (A)	RUCO Adjustments (B)	RUCO Proposed (C)
1	Gross Utility Plant in Service	\$ 35,931,696	\$ 1,052,065	\$ 36,983,761
2	Accumulated Depreciation	\$ (19,183,739)	\$ (630,244)	\$ (19,813,983)
3	<b>Net Utility Plant in Service</b>	<b>\$ 16,747,956</b>	<b>\$ 421,821</b>	<b>\$ 17,169,777</b>
<b>Less:</b>				
4	Advances in Aid of Construction	\$ (145,453)	\$ -	\$ (145,453)
5	Contributions in Aid of Construction (net of amortization)	\$ (4,747)	\$ -	\$ (4,747)
6	Imputed Regulatory Advances	\$ -	\$ -	\$ -
7	Imputed Regulatory Contributions	\$ (443,212)	\$ -	\$ (443,212)
10	Deferred Income Taxes and Credits	\$ 1,243,135	\$ (32,077)	\$ 1,211,058
11	Investment Tax Credits and Other Deferred Credits	\$ -	\$ -	\$ -
12	<b>Total Reductions</b>	<b>\$ 649,723</b>	<b>\$ (32,077)</b>	<b>\$ 617,646</b>
<b>Plus:</b>				
13	Unamortized Finance Charges	\$ -	\$ -	\$ -
14	Deferred Tax Assets	\$ -	\$ -	\$ -
15	Deferred Debits	\$ 108,771	\$ -	\$ 108,771
16	Allowance for Working Capital	\$ 314,822	\$ (113,000)	\$ 201,822
17	Utility Plant Acquisition Adjustment	\$ -	\$ -	\$ -
18	<b>Total Additions</b>	<b>\$ 423,593</b>	<b>\$ (113,000)</b>	<b>\$ 310,593</b>
19	<b>Total Rate Base</b>	<b>\$ 17,821,272</b>	<b>\$ 276,744</b>	<b>\$ 18,098,016</b>

Notes and Source

Col.A: AAWC Filing, Schedule B-1

Col.B: Schedule B.1

Arizona American Water Company - Sun City West Wastewater  
Summary of Adjustments to Rate Base

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule B.1 (SCW)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	RUCO Adjustments	Contributions in Aid of Construction		Cash Working Capital	Comprehensive Planning Study		Allocation of NWVTP		Accumulated Deferred Income Taxes	
			B-3	B-3	B-4 Revised	B-7 New	B-7 New	B-8 New	B-8 New	B-9 New	B-9 New
1	Gross Utility Plant in Service	\$ 1,052,065				\$ 12,242	\$ 12,242	\$ 1,039,823			
2	Accumulated Depreciation	\$ (630,244)						\$ (630,244)			
3	<b>Net Utility Plant in Service</b>	<b>\$ 421,821</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 12,242</b>	<b>\$ 12,242</b>	<b>\$ 409,579</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>
<b>Less:</b>											
4	Advances in Aid of Construction	\$ -									
5	Contributions in Aid of Construction (net of amortization)	\$ -	\$ -								
6	Imputed Regulatory Advances	\$ -									
7	Imputed Regulatory Contributions	\$ -									
10	Deferred Income Taxes and Credits	\$ (32,077)								\$ (32,077)	
11	Investment Tax Credits and Other Deferred Credits	\$ -									
12	<b>Total Reductions</b>	<b>\$ (32,077)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (32,077)</b>	<b>\$ -</b>
<b>Plus:</b>											
13	Unamortized Finance Charges	\$ -									
14	Deferred Tax Assets	\$ -									
15	Deferred Debits	\$ -									
16	Allowance for Working Capital	\$ (113,000)			\$ (113,000)						
17	Utility Plant Acquisition Adjustment	\$ -									
18	<b>Total Additions</b>	<b>\$ (113,000)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (113,000)</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>
18	<b>Total Rate Base</b>	<b>\$ 276,744</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ (113,000)</b>	<b>\$ 12,242</b>	<b>\$ 12,242</b>	<b>\$ 409,579</b>	<b>\$ (32,077)</b>	<b>\$ (32,077)</b>	<b>\$ -</b>

Notes and Source

See referenced exhibit for each adjustment



Arizona American Water Company - Sun City West Wastewater  
Adjusted Net Operating Income

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule C (SCW)  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Per Company (A)	RUCO Adjustments (B)	Per RUCO (C)
<b>Revenues</b>				
1	Sewer Revenues	\$ 5,660,389	\$ -	\$ 5,660,389
2	Other Revenues	\$ 1,321	\$ -	\$ 1,321
3	<b>Total Revenues</b>	<u>\$ 5,661,710</u>	<u>\$ -</u>	<u>\$ 5,661,710</u>
<b>Operating Expenses</b>				
4	Labor	\$ 766,759	\$ (21,079)	\$ 745,680
5	Purchased Water	\$ 7,156	\$ -	\$ 7,156
6	Fuel & Power	\$ 385,512	\$ -	\$ 385,512
7	Chemicals	\$ 401,682	\$ -	\$ 401,682
8	Waste Disposal	\$ 103,272	\$ -	\$ 103,272
9	Management Fees	\$ 789,604	\$ (106,197)	\$ 683,407
10	Group Insurance	\$ 267,064	\$ (1,386)	\$ 265,678
11	Pensions	\$ 150,285	\$ (50,830)	\$ 99,455
12	Regulatory Expense	\$ 43,794	\$ (18,954)	\$ 24,840
13	Insurance Other Than Group	\$ 48,786	\$ -	\$ 48,786
14	Customer Accounting	\$ 123,968	\$ -	\$ 123,968
15	Rents	\$ 38,079	\$ -	\$ 38,079
16	General Office Expense	\$ 49,950	\$ -	\$ 49,950
17	Miscellaneous	\$ 243,174	\$ (2,216)	\$ 240,958
18	Maintenance Expense	\$ 138,620	\$ -	\$ 138,620
19	Depreciation & Amortization	\$ 1,238,799	\$ -	\$ 1,238,799
20	General Taxes - Property Taxes	\$ 135,172	\$ -	\$ 135,172
21	General Taxes - Other	\$ 58,909	\$ -	\$ 58,909
22	Income Taxes	\$ 52,682	\$ 70,477	\$ 123,159
23	<b>Total Operating Expenses</b>	<u>\$ 5,043,267</u>	<u>\$ (130,186)</u>	<u>\$ 4,913,081</u>
24	<b>Utility Operating Income</b>	<u>\$ 618,443</u>	<u>\$ 130,186</u>	<u>\$ 748,629</u>
<b>Other Income &amp; Deductions</b>				
25	Other Income & Deductions	\$ -	\$ -	\$ -
26	Interest Expense	\$ (534,638)	\$ -	\$ (534,638)
27	Other Expense	\$ (9,599)	\$ -	\$ (9,599)
28	Gain/Loss Sale of Fixed Assets	\$ 2	\$ -	\$ 2
29	<b>Total Other Additions/Deductions From Income</b>	<u>\$ (544,235)</u>	<u>\$ -</u>	<u>\$ (544,235)</u>
30	<b>Net Profit (Loss)</b>	<u>\$ 74,208</u>	<u>\$ 130,186</u>	<u>\$ 204,394</u>
31	<b>Rate Base</b>	<u>\$ 17,821,272</u>	<u>\$ 276,744</u>	<u>\$ 18,098,016</u>
32	<b>Earned Rate of Return</b>	<u>3.47%</u>		<u>4.14%</u>

Notes and Source

Col.A: AAWC Filing, Schedule C-1  
Col.B: Schedule C.1  
Col.C: Col.A + Col.B

Arizona American Water Company - Sun City West Wastewater  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	RUCO Adjustments	Rate Case Expense C-2	Achievement Incentive Pay C-3	Stock-Based Compensation C-4	Pension Expense C-5	OPEB Expense C-6
<b>Revenues</b>							
1	Sewer Revenues	\$ -					
2	Other Revenues	\$ -					
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Operating Expenses</b>							
4	Labor	\$ (21,079)		\$ (14,441)	\$ (6,638)		
5	Purchased Water	\$ -					
6	Fuel & Power	\$ -					
7	Chemicals	\$ -					
8	Waste Disposal	\$ -					
9	Management Fees	\$ (106,197)			\$ (4,442)		\$ (1,386)
10	Group Insurance	\$ (1,386)					
11	Pensions	\$ (50,830)					
12	Regulatory Expense	\$ (18,954)	\$ (18,954)			\$ (50,830)	
13	Insurance Other Than Group	\$ -					
14	Customer Accounting	\$ -					
15	Rents	\$ -					
16	General Office Expense	\$ -					
17	Miscellaneous	\$ (2,216)					
18	Maintenance Expense	\$ -					
19	Depreciation & Amortization	\$ -					
20	General Taxes - Property Taxes	\$ -					
21	General Taxes - Other	\$ -					
15	PRE-TAX OPERATING EXPENSES	\$ (200,663)	\$ (18,954)	\$ (14,441)	\$ (11,080)	\$ (50,830)	\$ (1,386)
16	PRE-TAX OPERATING INCOME	\$ 200,663	\$ 18,954	\$ 14,441	\$ 11,080	\$ 50,830	\$ 1,386
17	Income Taxes	\$ 70,477	\$ 7,316	\$ 5,574	\$ 4,277	\$ 19,620	\$ 535
18	TOTAL OPERATING EXPENSES	\$ (130,186)	\$ (11,638)	\$ (8,867)	\$ (6,803)	\$ (31,210)	\$ (851)
19	OPERATING INCOME	\$ 130,186	\$ 11,638	\$ 8,867	\$ 6,803	\$ 31,210	\$ 851

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3 38.60%

Line No.	Description	Dues, Donations & Miscellaneous Expenses				Management Fees - 4% Post-Test Year Wage Increase		Management Fees - Affiliate Employee Benefits		Management Fees - Affiliate Incentive Compensation		Management Fees - Normalized Affiliate Pension Expense	
		C-7	C-9	C-9A	C-10	C-11	C-12	C-7	C-9	C-9A	C-10	C-11	C-12

## Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3

Arizona American Water Company - Sun City West Wastewater  
Summary of Net Operating Income Adjustments

Test Year Ended March 31, 2008

Line No.	Description	Management Fees - Normalize Affiliate OPEB Expense C-13	Management Fees - Remove Business Development Expenses C-14	Interest Synchronization C-15 Revised
<b>Revenues</b>				
1	Sewer Revenues			
2	Other Revenues			
3	<b>Total Revenues</b>	\$ -	\$ -	\$ -
<b>Operating Expenses</b>				
4	Labor			
5	Purchased Water			
6	Fuel & Power			
7	Chemicals			
8	Waste Disposal			
9	Management Fees			
10	Group Insurance			
11	Pensions			
12	Regulatory Expense			
13	Insurance Other Than Group			
14	Customer Accounting			
15	Rents			
16	General Office Expense			
17	Miscellaneous			
18	Maintenance Expense			
19	Depreciation & Amortization			
20	General Taxes - Property Taxes			
21	General Taxes - Other			
15	PRE-TAX OPERATING EXPENSES	\$ (961)	\$ (6,435)	\$ -
16	PRE-TAX OPERATING INCOME	\$ 961	\$ 6,435	\$ -
17	Income Taxes	\$ 371	\$ 2,484	\$ (6,977)
18	TOTAL OPERATING EXPENSES	\$ (590)	\$ (3,951)	\$ (6,977)
19	OPERATING INCOME	\$ 590	\$ 3,951	\$ 6,977

Notes and Source

Combined Effective Tax Rate per AAWC filing, Schedule C-3

Arizona American Water Company  
 Plant Retirements - Anthem/Agua Fria Wastewater

Test Year Ended December 31, 2008

Attachment RCS-7  
 Schedule B-2  
 Docket No. SW-01303A-09-0343  
 Page 1 of 1

Line No.	Description	Amount (A)	Reference
1	Remove Two 75-HP Final Effluent Pumps From Utility Plant in Service	\$ (52,636)	A
2	Reduce Accumulated Depreciation to Reflect the Retirement of Two 75-HP Final Effluent Pumps	\$ 52,636	
3	Net Adjustment to Utility Plant in Service	\$ -	

Notes and Source

A: Amount per AAWC's response to STF 7.3

Arizona American Water Company  
Cash Working Capital

Test Year Ended December 31, 2008

Attachment RCS-7  
Schedule B-4  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Anthem/Agua Fria Wastewater (A)		Sun City Wastewater (B)		Sun City West Wastewater (C)		Total Wastewater (D)		Reference
1	Cash Working Capital Requirement Per Filing	\$	285,666	\$	129,827	\$	229,465	\$	644,958	A
2	RUCO Recommended Cash Working Capital Requirement	\$	155,688	\$	24,767	\$	116,681	\$	297,136	B
3	Adjustment to Cash Working Capital	\$	(129,978)	\$	(105,060)	\$	(112,784)	\$	(347,822)	
4	Adjustment to Cash Working Capital Rounded to Nearest \$000	\$	(130,000)	\$	(105,000)	\$	(113,000)	\$	(348,000)	

Notes and Source

A: AAWC filing, Schedule B-6

B: See Schedules B-4 (AAF), B-4 (SC) and B-4 (SCW)

Test Year Ended December 31, 2008

Line No.	Test Year Adjusted Results (A)	RUCO Adjustments (B)	RUCO Adjusted (C)	Revenue Lag Days (D)	Expense Lag Days (E)	Net Lag Days (F)	Lead/Lag Factor (G)	Cash Working Capital Required (H)	Reference
<b>OPERATING EXPENSES</b>									
1	P08 Labor	\$ 1,335,278	\$ (30,484)	\$ 1,304,794	39.96	12.00	0.0766	\$ 99,947	
2	P09 Purchased Water	\$ 3,368	\$	\$ 3,368	39.96	52.52	(0.0344)	\$ (116)	
3	P10 Fuel & Power	\$ 278,664	\$	\$ 278,664	39.96	23.46	0.0452	\$ 12,596	
4	P11 Chemicals	\$ 303,374	\$	\$ 303,374	39.96	14.63	-	\$ -	b
5	P12 Waste disposal	\$ 199,095	\$	\$ 199,095	39.96	26.90	0.0358	\$ 7,124	
6	P13 Management Fees	\$ 1,528,005	\$ (205,507)	\$ 1,322,498	39.96	12.00	0.0766	\$ 101,303	a
7	P14 Group Insurance	\$ 396,599	\$ (2,682)	\$ 393,917	39.96	(13.70)	0.1470	\$ 57,914	
8	P15 Pensions	\$ 221,640	\$ (72,483)	\$ 149,157	39.96	(2.37)	0.1160	\$ 17,297	
9	P17 Insurance Other Than Group	\$ 94,566	\$	\$ 94,566	39.96	(83.68)	0.3387	\$ 32,034	
10	P18 Customer Accounting	\$ 242,170	\$	\$ 242,170	39.96	20.31	0.0538	\$ 13,037	c
11	P19 Rents	\$ 84,483	\$	\$ 84,483	39.96	(84.16)	0.3401	\$ 28,729	
12	P21 Miscellaneous	\$ 534,489	\$	\$ 534,489	39.96	16.84	0.0633	\$ 33,858	
13	P25 Maintenance Expense	\$ 246,204	\$	\$ 246,204	39.96	18.24	0.0595	\$ 14,651	
14	Other Operating Expenses	\$ 166,636	\$ (35,968)	\$ 130,668	39.96	30.00	0.0273	\$ 3,565	
15	P29 Property Taxes	\$ 296,804	\$	\$ 296,804	39.96	191.37	(0.4148)	\$ (123,123)	
16	P29 Taxes Other than Income	\$ 87,538	\$	\$ 87,538	39.96	13.35	0.0729	\$ 6,383	
17	P30 Income Tax	\$ 1,659,460	\$ 2,111,853	\$ 3,771,313	39.96	30.13	0.0269	\$ 101,557	
18	P56 Interest Sync	\$ 1,432,072	\$ (49,681)	\$ 1,382,391	39.96	106.25	(0.1816)	\$ (251,069)	
19	Working Cash Requirement	\$ 9,110,446	\$ 1,715,049	\$ 10,825,495				\$ 155,688	
20	Working Cash Requirement per Company							\$ 285,666	
21	Adjustment to Cash Working Capital							\$ (129,978)	

Notes and Source  
AAWC Filing, Schedule B-6

Col. D: RUCO recommending revenue lag days of 39.96. Company used 46.04 revenue lag days  
a: RUCO recommending 12 expense lag days for management fees. Company used 14.77 expense lag days  
b: The Company accepted Staff's adjustment to remove chemical expense from its CWC calculation  
c: The Company accepted Staff's adjustment to remove bad debt expense from Customer Accounting Expense

Line 17, Col. C, Current Income Taxes:

23	Per AAWC	\$ 1,659,460	
24	RUCO adjustments to current income taxes	\$ 149,098	Schedule C.1 (AAF), line 17
25	Income Taxes for Revenue Increase	\$ 1,962,755	Schedule A-1 (AAF), lines 12 & 13
26	Total current income taxes for CWC calculation	\$ 3,771,313	

Test Year Ended December 31, 2008

Line No.	Test Year Adjusted Results (A)	RUCO Adjustments (B)	RUCO Adjusted (C)	Revenue Lag Days (D)	Expense Lag Days (E)	Net Lag Days (F)	Lead/Lag Factor (G)	Working Capital Required (H)
<b>OPERATING EXPENSES</b>								
1 P08 Labor	\$ 454,529	\$ (18,617)	\$ 435,912	39.65	12.00	27.65	0.0758	\$ 33,024
2 P10 Fuel & Power	\$ 15,804	\$	\$ 15,804	39.65	20.75	18.91	0.0518	\$ 819
3 P11 Chemicals	\$ 4,885	\$	\$ 4,885	39.65	20.35	-	-	\$ -
4 P12 Waste Disposal	\$ 3,300,475	\$	\$ 3,300,475	39.65	43.73	(4.08)	(0.0112)	\$ (36,919)
5 P13 Management Fees	\$ 933,155	\$ (125,503)	\$ 807,652	39.65	12.00	27.65	0.0758	\$ 61,187
6 P14 Group Insurance	\$ 141,193	\$ (1,638)	\$ 139,555	39.65	(13.67)	53.32	0.1461	\$ 20,388
7 P15 Pensions	\$ 75,595	\$ (25,187)	\$ 50,408	39.65	(2.37)	42.02	0.1151	\$ 5,803
8 P17 Insurance Other Than Group	\$ 57,656	\$	\$ 57,656	39.65	(83.68)	123.34	0.3379	\$ 19,482
9 P18 Customer Accounting	\$ 145,686	\$	\$ 145,686	39.65	20.31	19.34	0.0530	\$ 7,720
10 P19 Rents	\$ 40,868	\$	\$ 40,868	39.65	(93.42)	133.08	0.3646	\$ 14,900
11 P21 Miscellaneous	\$ 104,503	\$	\$ 104,503	39.65	12.47	27.18	0.0745	\$ 7,782
12 P25 Maintenance Expense	\$ 61,533	\$	\$ 61,533	39.65	29.75	9.91	0.0271	\$ 1,670
13 Other Operating Expenses	\$ 94,627	\$ (23,193)	\$ 71,434	39.65	30.00	9.65	0.0264	\$ 1,889
14 P29 Property Taxes	\$ 157,456	\$	\$ 157,456	39.65	189.67	(150.02)	(0.4110)	\$ (64,716)
15 P29 Taxes Other than Income	\$ 34,880	\$	\$ 34,880	39.65	13.35	26.31	0.0721	\$ 2,514
16 P30 Income Tax	\$ 513,251	\$ 658,109	\$ 1,171,360	39.65	30.13	9.52	0.0261	\$ 30,558
17 P56 Interest	\$ 442,923	\$ 2,840	\$ 445,763	39.65	106.25	(66.60)	(0.1825)	\$ (81,334)
18 Total	\$ 6,579,018	\$ 466,811	\$ 7,045,829					
19 Working Cash Requirement								\$ 24,767
20 Working Cash Requirement per Company								\$ 129,827
21 Adjustment to Cash Working Capital								\$ (105,060)

Notes and Source

AAWC Filing, Schedule B-6  
Col. D: RUCO recommending revenue lag days of 39.65. Company used 45.74 revenue lag days  
a: RUCO recommending 12 expense lag days for management fees. Company used 14.77 expense lag days  
b: The Company accepted Staff's adjustment to remove chemical expense from its CWC calculation  
c: The Company accepted Staff's adjustment to remove bad debt expense from Customer Accounting Expense

Line 17, Col. C, Current Income Taxes:

23 Per AAWC	\$ 513,251
24 RUCO adjustments to current income taxes	\$ 73,841
25 Income Taxes for Revenue Increase	\$ 584,268
26 Total current income taxes for CWC calculation	\$ 1,171,360



Test Year Ended December 31, 2008

Line No.	Test Year Adjusted Results (A)	RUCO Adjustments (B)	RUCO Adjusted (C)	Revenue Lag Days (D)	Expense Lag Days (E)	Net Lag Days (F)	Lead/Lag Factor (G)	Cash Working Capital Required (H)	Reference
<b>OPERATING EXPENSES</b>									
1	P08 Labor	\$ 766,759	\$ (21,079)	\$ 745,680	39.61	12.00	0.0756	\$ 56,406	
2	P09 Purchased Water	\$ 7,156	\$ 7,156	\$ 7,156	39.61	52.52	(0.0354)	\$ (253)	
3	P10 Fuel & Power	\$ 385,512	\$ 385,512	\$ 385,512	39.61	23.18	0.0450	\$ 17,350	
4	P11 Chemicals	\$ 401,682	\$ 401,682	\$ 401,682	39.61	17.28	-	\$ -	b
5	P12 Waste Disposal	\$ 103,272	\$ 103,272	\$ 103,272	39.61	19.93	0.0539	\$ 5,568	
6	P13 Management Fees	\$ 789,604	\$ (106,197)	\$ 683,407	39.61	12.00	0.0756	\$ 51,695	a
7	P14 Group Insurance	\$ 267,064	\$ (1,386)	\$ 265,678	39.61	(13.62)	0.1458	\$ 38,742	
8	P15 Pensions	\$ 150,285	\$ (50,830)	\$ 99,455	39.61	(2.37)	0.1150	\$ 11,438	
9	P17 Insurance Other Than Group	\$ 48,786	\$ 48,786	\$ 48,786	39.61	(83.68)	0.3378	\$ 16,480	
10	P18 Customer Accounting	\$ 123,968	\$ 123,968	\$ 123,968	39.61	20.31	0.0529	\$ 6,555	c
11	P19 Rents	\$ 38,079	\$ 38,079	\$ 38,079	39.61	(72.11)	0.3061	\$ 11,655	
12	P21 Miscellaneous	\$ 243,174	\$ 243,174	\$ 243,174	39.61	29,7026	0.0814	\$ 19,789	
13	P25 Maintenance Expense	\$ 138,620	\$ 138,620	\$ 138,620	39.61	26.14	0.0369	\$ 5,117	
14	Other Operating Expenses	\$ 93,744	\$ (21,170)	\$ 72,574	39.61	30.00	0.0263	\$ 1,911	
15	P29 Property Taxes	\$ 135,000	\$ 135,000	\$ 135,000	39.61	187.98	(0.4065)	\$ (54,878)	
16	P29 Taxes Other than Income	\$ 58,909	\$ 58,909	\$ 58,909	39.61	13.35	0.0720	\$ 4,239	
17	P30 Income Tax	\$ 619,532	\$ 373,036	\$ 992,568	39.61	30.13	0.0260	\$ 25,780	
18	P56 Interest Sync	\$ 534,640	\$ 18,073	\$ 552,713	39.61	106.25	(0.1826)	\$ (100,912)	
19	Total	\$ 4,905,786	\$ 190,447	\$ 5,096,232					
20	Working Cash Requirement							\$ 116,681	
21	Working Cash Requirement per Company							\$ 229,465	
22	Adjustment to Cash Working Capital							\$ (112,784)	

Notes and Source

AAWC Filing, Schedule B-6

Col. D: RUCO recommending revenue lag days of 39.61. Company used 45.63 revenue lag days

a: RUCO recommending 12 expense lag days for management fees. Company used 14.77 expense lag days

b: The Company accepted Staff's adjustment to remove chemical expense from its CWC calculation

c: The Company accepted Staff's adjustment to remove bad debt expense from Customer Accounting Expense

Line 17: Col. C: Current Income Taxes:

23	Per AAWC	\$ 619,532	Schedule C.1 (SCW), line 17
24	RUCO adjustments to current income taxes	\$ 70,477	Schedule A-1 (SCW), lines 12 & 13
25	Income Taxes for Revenue Increase	\$ 302,559	
26	Total current income taxes for CWC calculation	\$ 992,568	

Arizona American Water Company  
Verrado Wastewater Plant - Anthem/Agua Fria Wastewater

Attachment RCS-7  
Schedule B-6  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
New

Test Year Ended December 31, 2008

Line No.	Description	Anthem/Agua Fria		Reference
		Wastewater	(A)	
1	Adjustment to Reduce Utility Plant in Service Related to the Verrado Wastewater Plant	\$	<u>(1,838,637)</u>	A

Notes and Source

A: AAWC accepted Staff's adjustment related to the Verrado Wastewater Plant per the rebuttal testimony of Company  
witness Sandra L. Murrey

Arizona American Water Company  
Comprehensive Planning Study

Attachment RCS-7  
Schedule B-7  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
New

Test Year Ended December 31, 2008

Line No.	Description	Amount (A)	Reference
1	Adjustment to Transfer Costs Associated With Planning Study From Sun City Wastewater	\$ (12,242)	A
2	Adjustment to Transfer Costs Associated With Planning Study to Sun City West Wastewater	\$ 12,242	A
3	Net Adjustment to Utility Plant in Service Related to Planning Study	\$ -	

Notes and Source

A: AAWC accepted Staff's adjustment related to the main planning study per the rebuttal testimony of Company witness Sandra L. Murrey

Line No.	Description	Amount (A)	Reference
<b>Utility Plant in Service</b>			
1	Adjustment to Revise Allocation of the NWWTP Related to Anthem/Agua Fria Wastewater	\$ (1,039,823)	A
2	Adjustment to Revise Allocation of the NWWTP Related to Sun City West Wastewater	\$ 1,039,823	A
3	Net Adjustment to Utility Plant in Service Related to the NWWTP	\$ -	
<b>Accumulated Depreciation</b>			
4	Adjustment to Revise Allocation of the NWWTP Related to Anthem/Agua Fria Wastewater	\$ 630,244	A
5	Adjustment to Revise Allocation of the NWWTP Related to Sun City West Wastewater	\$ (630,244)	A
6	Net Adjustment to Accumulated Depreciation in Service Related to the NWWTP	\$ -	

**Notes and Source**

A: AAWC accepted Staff's adjustments related to the NWWTP per the rebuttal testimony of Company witness Linda J. Gutowski

Test Year Ended December 31, 2008

Line No.	Description	Anthem/Agua Fria Wastewater (A)	Sun City Wastewater (B)	Sun City West Wastewater (C)	Total Wastewater (D)	Reference
1	Estimated Normalized Rate Case Expense Per Filing	\$ 72,069	\$ 44,090	\$ 39,060	\$ 155,219	A
2	RUCO Recommended Normalized Rate Case Expense	\$ 40,390	\$ 23,517	\$ 20,106	\$ 84,013	B
3	Adjustment to Rate Case Expense	\$ (31,679)	\$ (20,573)	\$ (18,954)	\$ (71,206)	L2 - L1

Notes and Source

A: AAWC estimated normalized rate case expense calculated as follows (amounts from Adjustment MHK-8 from AAWC filing):

4	Estimated Rate Case Expense per Company	Anthem/Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater
5	Normalized over three years	\$ 678,425	\$ 678,425	\$ 678,425
6	Estimated Normalized Rate Case Expense	\$ 226,142	\$ 226,142	\$ 226,142
7	2009 Group 4-Factor per Company	26.341%	15.337%	13.113%
8	Allocated Rate Case Expense	\$ 59,569	\$ 34,684	\$ 29,654
9	Unamortized Balance of Prior Rate Case Expense	\$ 37,500	\$ 28,218	\$ 28,218
10	Normalized over three years	\$ 12,500	\$ 9,406	\$ 9,406
11	Annual Amortization of Unamortized Rate Case Expense			
12	Pro Forma Rate Case Expense	\$ 72,069	\$ 44,090	\$ 39,060

B: RUCO recommended Rate Case Expense calculated as follows:

13	RUCO recommended Rate Case Expense	\$ 460,000	\$ 460,000	\$ 460,000
14	Normalized over three years	\$ 153,333	\$ 153,333	\$ 153,333
15	Normalized Rate Case Expense	26.341%	15.337%	13.113%
16	2009 Group 4-Factor	\$ 40,390	\$ 23,517	\$ 20,106
17	Allocated Rate Case Expense			

Arizona American Water Company  
Achievement Incentive Pay

Attachment RCS-7  
Schedule C-3  
Docket No. SW-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	(A)		(B)		(C)		(D)		Reference
		Anthem/Agua Fria Wastewater	Sun City Wastewater	Sun City Wastewater	Sun City West Wastewater	Total Wastewater	Total Wastewater			
1	Achievement Incentive Pay Recorded at 12/31/2008	\$ -	\$ -	\$ -	\$ 17,753	\$ 17,753			A	
2	Corporate Allocation	\$ 58,795	\$ 35,906	\$ 35,906	\$ 30,382	\$ 125,083			A&B	
3	Total Achievement Incentive Pay	\$ 58,795	\$ 35,906	\$ 35,906	\$ 48,135	\$ 142,836				
4	Disallowance Percentage	30%	30%	30%	30%				C	
5	Adjustment to Achievement Incentive Pay	\$ (17,639)	\$ (10,772)	\$ (10,772)	\$ (14,441)	\$ (42,852)				

Notes and Source

- A: Amounts above per Company workpaper "AI-2008" for each district  
B: Corporate allocation amounts also provided in AAWC's responses to RUCO 2-6 and RUCO 3-2  
C: Testimony of RUCO witness Ralph Smith

Test Year Ended December 31, 2008

Line No.	Description	Anthem/Agua Fria Wastewater (A)	Sun City Wastewater (B)	Sun City West Wastewater (C)	Total Wastewater (D)	Reference
1	Adjustment to Remove Stock-Based Compensation - Management Fees	\$ (8,595)	\$ (5,249)	\$ (4,442)	\$ (18,286)	A
2	Adjustment to Remove Stock-Based Compensation - Labor	\$ (12,845)	\$ (7,845)	\$ (6,638)	\$ (27,328)	A
3	Total Adjustment to Remove Stock-Based Compensation	<u>\$ (21,440)</u>	<u>\$ (13,094)</u>	<u>\$ (11,080)</u>	<u>\$ (45,614)</u>	

Notes and Source

A: Amounts below from AAWC's supplemental response to RUCO 6-3

Description	Service Company Portion	AAWC Non-Affiliate Portion	Total
4 Comp - Stock Options - Account 501716	\$ 36,693		\$ 36,693
5 Comp - Restricted Stock - Account 501717	\$ 28,834	\$ 103,974	\$ 132,808
6 Comp - Restricted Stock Units - Account 701718	\$ 4,046		\$ 4,046
7 Total Test Year Stock-Based Compensation	<u>\$ 69,573</u>	<u>\$ 103,974</u>	<u>\$ 173,547</u>
<b>Service Company Portion</b>			
8 Total Test Year Stock-Based Compensation - Service Company Portion	Anthem/Agua Fria Wastewater	Sun City Wastewater	Sun City West Wastewater
9 4-Factor Allocator	\$ 69,573	\$ 69,573	\$ 69,573
10 Total Allocated Test Year Stock-Based Compensation - Service Company Portion	<u>12.354%</u>	<u>7.545%</u>	<u>6.3842%</u>
	<u>\$ 8,595</u>	<u>\$ 5,249</u>	<u>\$ 4,442</u>
<b>Non-Affiliate Portion</b>			
11 Total Test Year Stock-Based Compensation - Non-Affiliate Portion	\$ 103,974	\$ 103,974	\$ 103,974
12 4-Factor Allocator	<u>12.354%</u>	<u>7.545%</u>	<u>6.384%</u>
13 Total Allocated Test Year Stock-Based Compensation - Non-Affiliate Portion	<u>\$ 12,845</u>	<u>\$ 7,845</u>	<u>\$ 6,638</u>

Arizona American Water Company  
Pension Expense

Attachment RCS-7  
Schedule C-5  
Docket No. SW-01303A-09-0343  
Page 1 of 1

Test Year Ended December 31, 2008

Line No.	Description	Anthem/Agua Fria Wastewater (A)	Sun City Wastewater (B)	Sun City West Wastewater (C)	Total Wastewater (D)	Reference
1	Pro Forma Pension Expense Per Filing	\$ 221,640	\$ 74,281	\$ 148,791	\$ 444,712	A
2	RUCO Recommended Pro Forma Pension Expense	\$ 149,157	\$ 49,094	\$ 97,961	\$ 296,212	B&C
3	Adjustment to Pension Expense	\$ (72,483)	\$ (25,187)	\$ (50,830)	\$ (148,500)	

Notes and Source

A: Per Schedule C-2, Adjustment No. SLH-2 from AAWC's filing

B: RUCO recommended pension expense calculated as follows (amounts from AAWC's response to RUCO 2-60):

	Amount
5 Recorded Pension Expense - 2007	\$ 903,222
6 Recorded Pension Expense - 2008	\$ 1,734,561
7 Subtotal	\$ 2,637,783
8 Normalized Over Two Years	2
9 Normalized Pension Expense	\$ 1,318,892

C: RUCO calculated its pension expense adjustment by incorporating the normalized amount above to Company workpaper "AZ 2008 Labor" as shown on pages 2 and 3 of this schedule



Test Year Ended December 31, 2008

Line No.	Description	Anthem/Agua Fria Wastewater (A)	Sun City Wastewater (B)	Sun City West Wastewater (C)	Total Wastewater (D)	Reference
1	Normalized OPEB Expense Per Filing (Expensed Portion)	\$ 78,238	\$ 78,238	\$ 78,238		A
2	4 Factor Allocation Factor	12.354%	7.545%	6.384%		
3	Adjusted Test Year OPEB Expense Per Company	\$ 9,666	\$ 5,903	\$ 4,995	\$ 20,564	
4	RUCO Recommended Pro Forma OPEB Expense	\$ 6,984	\$ 4,265	\$ 3,609	\$ 14,858	
5	Adjustment to OPEB Expense	\$ (2,682)	\$ (1,638)	\$ (1,386)	\$ (5,706)	

Notes and Source

A: Per Schedule C-2, Adjustment No. SLH-14 from AAWC's filing

B: RUCO recommended pension expense calculated as follows (amounts from AAWC's response to RUCO 2-60):

	Amount
7 Recorded OPEB Amount - 2007	\$ 62,603
8 Recorded OPEB Amount - 2008	\$ 75,723
9 Subtotal	\$ 138,326
10 Normalized Over Two Years	2
11 Normalized OPEB Cost	\$ 69,163
12 Capitalization Percentage	18.3%
13 Capitalized Portion of OPEB Cost	\$ (12,634)
14 Expensed Portion of OPEB Cost	\$ 56,529 L11 + L13
15 4 Factor Allocation Factor	12.354%
16 Anthem/Agua Fria Wastewater Portion of OPEB Expense	\$ 6,984 L14 x L15
17 4 Factor Allocation Factor	7.545%
18 Sun City Wastewater Portion of OPEB Expense	\$ 4,265 L14 x L17
21 4 Factor Allocation Factor	6.384%
22 Sun City West Wastewater Portion of OPEB Expense	\$ 3,609 L14 x L21

Arizona American Water Company  
Interest Synchronization

Test Year Ended December 31, 2008  
(Thousands of Dollars)

Attachment RCS-7  
Schedule C-15  
Docket No. SW-01303A-09-0343  
Page 1 of 1  
Revised

Line No.	Description	Anthem/Aqua Fria		Sun City		Sun City West		Total		Reference
		Wastewater	(A)	Wastewater	(B)	Wastewater	(C)	Wastewater	(D)	
1	Adjusted Rate Base, per RUCO	\$ 45,264,942		\$ 14,596,027		\$ 18,098,016		\$ 77,958,985		Schedules B (AAF), B (SC) and B (SCW)
2	Weighted Cost of Debt, per RUCO	3.05%		3.05%		3.05%				Per RUCO - Schedule D
3	Interest Deduction for Tax Purposes	\$ 1,382,391		\$ 445,763		\$ 552,713		\$ 2,380,867		L1 x L2
4	Interest Deduction per Company	\$ 1,432,072		\$ 442,923		\$ 534,638		\$ 2,409,633		Note A
5	Difference (Decreased) Increased Interest Deduction	\$ (49,681)		\$ 2,840		\$ 18,075		\$ (28,766)		L3 - L4
6	Combined Federal and State Income Tax Rates	38.60%		38.60%		38.60%				L5 x L6
7	Increase (Decrease) to Income Tax	\$ 19,177		\$ (1,096)		\$ (6,977)		\$ 11,104		

Notes and Source

A: AAWC Filing, Schedule C-1 (line 32) for each wastewater district referenced above

Arizona American Water Company  
 Depreciation Expense - Anthem/Agua Fria Wastewater

Test Year Ended December 31, 2008

Attachment RCS-7  
 Schedule C-17  
 Docket No. SW-01303A-09-0343  
 Page 1 of 1

Line No.	Description	Amount (A)	Reference
1	Two 75-HP Final Effluent Pumps Removed From Utility Plant in Service	\$ (52,636)	A
2	Depreciation Rate	5.42%	B
3	Adjustment to Depreciation Expense	<u>\$ (2,853)</u>	

Notes and Source

A: See Exhibit LA-1, Schedule B-1

B: Depreciation rate taken from rate base Adjustment No. SLM-1 from AAWC's filing

Arizona American Water Company  
 Depreciation Expense - Anthem/Agua Fria Wastewater Reclassified Accounts

Attachment RCS-6  
 Schedule C-19  
 Docket No. SW-01303A-09-0343  
 Page 1 of 1  
 New

Test Year Ended December 31, 2008

Line No.	Account	Description	Amount (A)	Depreciation Rate* (B)	Depreciation Expense (C)	Reference
1	354400	Wastewater Structures & Improvements	\$ (487,000)	1.67%	\$ (8,133)	A
2	355500	Power Generation Equipment	\$ 487,000	4.42%	\$ 21,525	A
3		Net Adjustment to Depreciation Expense			<u>\$ 13,392</u>	

Notes and Source

A: These adjustments to depreciation expense reflect the impact of Staff's adjustment to reclassify the amount in Column A between the referenced accounts as discussed in the Rebuttal Testimony of Company witness Sandra L. Murrey

\* Depreciation rates from revised Company Adjustment SLM-1

**Arizona-American Water Company**  
**Docket No. W-01303A-09-0343 & SW-01303A-09-0343**  
**Attachment RCS-8**  
**Copies of AAWC's Responses to Data Requests**  
**and Documents Referenced in the Surrebuttal Testimony and Schedules of**  
**Ralph C. Smith**

<b>Data Request/ Workpaper No.</b>	<b>Subject</b>	<b>Confidential</b>	<b>No. of Pages</b>	<b>Page No.</b>
	Excerpt of IAWC President Teasley's Direct Testimony in Illinois Docket No. 09-0319	No	3	2 - 4
	Excerpt of Final Order in West Virginia Case No. 08-1783-G-42T, dated November 20, 2009	No	7	5 - 11
RUCO 7-1	Treatment of pension accruals and contributions for ratemaking purposes (without attachment)	No	1	12
	Total Pages Including this Page		12	

**ILLINOIS COMMERCE COMMISSION**

**IAWC EXHIBIT 1.00**

**DIRECT TESTIMONY OF**

**KARLA O. TEASLEY**

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**ILLINOIS-AMERICAN WATER COMPANY**

**DIRECT TESTIMONY  
OF  
KARLA O. TEASLEY**

**EXHIBIT NO. 1.00**

**I. WITNESS IDENTIFICATION AND BACKGROUND**

**Q1. Please state your name.**

**A.** My name is Karla O. Teasley.

**Q2. Please state your business address.**

**A.** 300 North Water Works Drive, Belleville, Illinois 62223.

**Q3. By whom are you employed and in what capacity?**

**A.** I am employed by Illinois-American Water Company ("IAWC" or "Company"), and serve as President of the Company.

**Q4. Please summarize your education and employment history.**

**A.** I hold a bachelor's degree from the University of Wisconsin (Eau Claire) and a Juris Doctor from the University of Minnesota Law School. I am a member of the bar in Minnesota and Florida, currently on inactive status in both states. I have been President of the Company since January 2007. Since graduating from law school in 1983, I have held increasingly responsible positions in the public utility industry. Between 1983 and 1989, I was a staff attorney for Minnesota Power based in Duluth, Minnesota. From 1989 through 1997, I was Vice President, General Counsel, Secretary and Director of Florida Water Services, a privately owned water and wastewater utility based in Orlando, Florida. In addition to my duties as Secretary for the Board of Directors, I provided all in-house legal services for the utility including contracts, regulatory affairs (including rate and environmental regulation), human resources, bond issues, eminent domain and real property. From 1997 through January 2007, I was a Vice President of Louisville Water Company in Louisville, Kentucky. When I left that position, I had

this proceeding on April 18, 2007 which ordered the Company to undertake the commitments agreed to in the stipulation. The Commission also ordered IAWC to take certain steps with regard to record keeping and reporting, customer service and communication, hydrant inspection, and billing.

**Q27. Have you prepared information regarding the status of the compliance with the Docket 05-0681 requirements?**

**A.** Yes. IAWC Exhibit 1.03 shows each requirement of the Docket 05-0681 Order, and indicates the status of the Company's compliance with each such requirement.

#### **VII. INCENTIVE COMPENSATION**

**Q28. Has the Company proposed recovery of expense related to payments under an incentive compensation plan?**

**A.** No. In the Docket 07-0507 Order, the Commission denied recovery of incentive compensation expense due to the presence of a parent company financial trigger. In recognition of the Commission's concern as stated in Docket 07-0507, IAWC will not pursue rate recovery of this cost.

#### **VIII. DEMAND AND COST-OF-SERVICE STUDIES**

**Q29. Did the Commission establish other requirements in the Docket 07-0507 Order issued in the Company's last rate case?**

**A.** Yes. In the Docket 07-0507 Order, the Commission required IAWC to, in its next rate proceeding, perform a Demand Study and Cost of Service Study and address several matters related to the design of IAWC's rates. Also, in the Docket 08-0463 Order, the Commission initiated a rate design investigation



081783comi112009.wpd

**PUBLIC SERVICE COMMISSION  
OF WEST VIRGINIA  
CHARLESTON**

At a session of the Public Service Commission of West Virginia, in the City of Charleston,  
on the 20th day of November 2009.

Case No. 08-1761-G-PC

HOPE GAS, INC., dba DOMINION HOPE,  
DOMINION RESOURCES, INC., and  
PEOPLES HOPE GAS COMPANIES, LLC,

Joint petition for consent and approval of the  
purchase and sale of the common stock of Hope  
Gas, Inc., and related relief.

Case No. 08-1783-G-42T

HOPE GAS, INC., dba DOMINION HOPE,  
a private utility, Clarksburg, Harrison County.

Rule 42T application to increase gas rates and  
charges.

**COMMISSION ORDER ON THE REQUEST  
FOR INCREASED RATES AND CHARGES**

Staff recommended calculating bad debt by using a three-year average from the years 2005-2007, yielding an uncollectible rate of 2.475%. Staff also adjusted the revenue amount applied to the uncollectible rate, but accepted a revised allowance for bad debt from Richwood Hospital. Staff Ex. 6A at 18-21.

The Commission agrees with the use of a three-year average to determine a reasonable going level uncollectible rate. We note that the use of a three-year average is consistent with prior precedent for calculating the amount of uncollectible accounts. 2008 WVAWC Order at 56-57. The average rate proposed by the CAD and Staff are nearly identical. The Commission is not convinced, however, that Hope will be able to collect the expenses from the Richwood Hospital in the bankruptcy proceeding. The Commission finds that the prudent course is for Hope to file a bankruptcy claim in the Richwood Hospital proceeding, but allow the revised three-year amortization of \$270,707 in the Commission revenue requirement calculation. Because the Staff calculations include the \$270,707, we will adopt Staff's calculation of going level uncollectibles. The Commission refuses to penalize Hope for providing service to a community hospital despite its financial difficulties, but in the future Hope should take reasonable steps to recover its losses including, at a minimum, filing a bankruptcy claim. In the event that Hope recovers all or part of the amounts owed in the bankruptcy proceeding, the Commission may adjust the amortization in a future rate case. In addition, that recovery may affect net write-offs to reduce average uncollectibles allowed in future cases.

#### 6. Out of Period Gasoline

Hope included \$125,538 in gasoline expenses in its calculation that it incurred outside of the test year. Staff and CAD each recommended that the Commission remove that amount from its calculation. Staff Ex. 6A at 21 and CAD Ex. At 43-44. Hope justified retaining the gasoline expenses in its calculation on price volatility. *Id.* The Commission notes that gasoline expenses have shown instability in the past few years, but more recently prices have stabilized. The Commission believes that there is a sufficient basis to adjust the cost actually incurred during the test year, but finds that allowing gasoline expenses within the cost of service calculation from outside the test year distorts the expenses Hope incurred. The Commission accepts the recommendation from Staff and CAD to remove the out of period gasoline expenses of \$125,538.

#### 7. Payroll and Benefit Expenses

##### a. Initial Positions

In its initial filing, Hope annualized actual salary figures from March 2008, the last month of the test year. Hope adjusted its annualized salary figures to include a base pay increase for salaried employees, union contract increases and incentive compensation for non-union employees. Hope Ex. 12 at 7. Hope also made adjustments to its revenue requirement calculations for various benefit cost increases, including medical, dental and insurance plans. *Id.* at 8.

CAD initially recommended a series of adjustments reducing the Hope calculations to reflect a lower employee count and a different approach to incentive compensation. CAD Ex. 9 at 54-59. CAD also initially suggested reversing an adjustment Hope made to OPEB expenses of \$33,440. Id. at 75-76.

Staff submitted a separate employee salary and benefit calculation based on an annualization of actual salary figures from February 2009, instead of March 2008. Staff calculated a gross annual base payroll of \$10,416,236 instead of the Hope figure of \$10,864,102. Staff Ex. 6A at 6. Staff then apportioned the gross payroll, with 14.26% assigned to capital accounts and 85.74% to O&M accounts, yielding a final Staff recommendation of \$8,930,881 in cost of service. Id. at 7.

Staff recommended rejecting a vacation accrual credit of \$92,680 (expensed to \$79,464) because it presented updated payroll figures from the Hope numbers. Id. Staff also recommended rejecting any further payroll adjustment for merit increases beyond that included in the February 2009 payroll numbers as speculative, eliminating \$93,479 (expensed to \$80,149). Id. at 7-8. Hope initially included a recommendation for a scheduled union contract increase on April 1, 2009 of \$297,832, but Staff calculated that increase at \$278,099, removing \$19,733 (expensed to \$16,919) from its calculation. Staff also included a prior union progression in its updated payroll calculation mooted an adjustment of \$9,818 (expensed to \$8,418). Id. at 9.

Staff also recommended reducing the FICA adjustment Hope proposed, arguing that Hope overstated its costs because not all employee salary is subject to employment taxes and other Hope salary calculations are inconsistent with its adjustment. Staff recommended adjusting going level FICA expenses by only \$20,858 instead of \$157,182. Staff also recommended reducing going level VEBA expenses for Hope by an additional \$16,913 to account for the updated payroll. Id. at 14. Finally, Hope proposed adjustments for a series of employee benefits including medical, dental, life insurance, savings plans and other miscellaneous benefits.<sup>4</sup> Id. at 15-17. Staff recommended reducing the combined Hope adjustment for these benefits of \$774,668 by \$271,666 for a total Staff recommended adjustment of \$503,002. Staff noted that its numbers were based on costs from 2009 while Hope derived its estimates from 2007 projections. Id.

Staff also recommended that the Commission reject the inclusion of a portion of the Hope incentive compensation program. Hope included an adjustment of \$366,823 in its payroll calculations for a three-year average of employee bonuses. The bonus program is based partially on corporate earnings goals and partially on operational goals for non-officers and solely earnings based for corporate officers. Id. at 9-11. Staff recommended reducing the bonus adjustment to a proportion of the goals Staff argued is operationally related, 35%, yielding a reduced adjustment of \$128,388. Staff also recommended rejecting a separate bonus category for corporate officers contained in expenses charged by the affiliated service company. Id. at 12. That charge is discussed at Section IV. E.14 below.

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<sup>4</sup> A discussion of the pension credit that Hope also included in this adjustment is discussed separately in Sections IV. D. 11 at IV. E. 2 above.

b. Payroll and Benefit Expenses - Agreement of the Parties

The parties subsequently agreed to most of the Staff proposal for calculating Hope payroll and benefit costs. In rebuttal testimony, Hope announced that it agreed with using payroll from February 2009 instead of the March 2008 figures Hope initially filed. Hope Ex. 10 at 2. Hope noted that using the Staff payroll calculation included the adjustment for a union progression Hope initially proposed and stated that the updated payroll figures eliminated the need for a vacation adjustment. *Id.* at 5-6. Hope also adopted the Staff figures on its VEBA adjustment and the calculations for benefits including medical, dental, life insurance, savings plans and miscellaneous benefits. *Id.* at 7-8. Finally, Hope also adopted the Staff FICA adjustment. Hope Ex. 14 at 13. Hope disagreed, however, with the method Staff recommended for handling annual bonus pay with an updated adjustment of \$330,017, and sought merit raises for non-officer salary employees for 2009. Hope Ex. 10 at 4, 6.

At hearing, CAD announced that it accepted the Staff proposal using February 2009 payroll calculations and associated benefit cost calculations. Tr. Vol. I at 110. CAD also decided to withdraw its recommendation to reverse a \$33,440 adjustment Hope made to OPEB expenses. *Id.* at 111.

Based on the testimony summarized above, the parties reached agreement on most payroll and benefit issues, adopting the Staff calculations annualizing February 2009 Hope payroll. The Commission accepts the recommendation of the parties on these issues and includes the February 2009 payroll and Staff adjustments on the agreed payroll issues into its cost of service calculation.

c. Merit Pay Increases

Hope continued to advocate for merit increases for its non-officer salary employees for 2009, characterizing the \$84,099 increase as a known and measurable change. Hope Ex. 10 at 6.

Staff, however, objected on the basis of a recent Commission decision denying a request to include similar non-officer salary expenses into the cost of service calculations because of the current economic climate. Staff Initial Brief at 14-16 and 2008 WVAWC Order at 51. CAD also opposed any additional merit increase based on the current economic climate, citing the same order. CAD Initial Brief at 89-90.

The Commission continues to view merit increases for non-officer salary positions as being questionable during periods of economic hardship and high unemployment. These salary increases, although known and reasonable, do not meet a prudence test given the financial conditions we are facing. With continuing financial turmoil in the national and global economy, the Commission rejects the necessity for ratepayers to bear this expense and excludes the adjustment Hope proposed.

#### d. Incentive Compensation

Hope advocated for the Commission to include the cost of its incentive compensation programs for direct Hope employees, arguing that the incentive plan encourages employees to set and achieve scored goals. It noted that its 2009 incentive compensation was not included in the Staff calculation because those incentives took effect in March 2009. Hope Ex. 10 at 4. Hope urged the Commission to include an adjustment from the February 2009 payroll figures, adding an additional \$330,017 for incentive compensation.

CAD urged the Commission to divide financial responsibility for incentive compensation costs equally between ratepayers and Dominion shareholders through the calculation. CAD argued that both ratepayers and shareholders benefit from the fruits of incentive compensation and both parties should pay for those expenses. It asserted that there is no assurance from Hope of future bonus payments to employees. CAD Initial Brief at 85-89. Staff also recommended dividing the cost of the incentive compensation plan between ratepayers and shareholders, but recommended that shareholders pay 65% of cost because Staff believed that 65% of the incentive goals tracked earnings goals instead of operations goals. Staff Ex. 6A at 11.

On the current record before us, the Commission finds that the incentive plan benefits ratepayers by providing incentives to Hope employees to meet improved operational goals. The Commission declines the invitations from CAD and Staff to mathematically quantify the percentage of the effect that the incentive program benefits Dominion shareholders versus ratepayers. As shown by the record in this matter and Hope arguments, emphasis from incentive goals shifts over time in response to differing priorities. The Commission will continue to allow the incentive program in its calculation, adopting Hope's adjustment of \$330,017.

#### 8. Interest on Customer Deposits

CAD suggested an adjustment reducing going level rate base by \$47,302 and increasing O&M expense by \$18,054 to reflect interest payments on customer deposits. CAD justified the adjustments on the basis that Hope reduced its rate base calculation by the amount of its customer deposits. CAD also noted that the Commission recently established a 1.00% interest rate on customer deposits in General Order 185.30. CAD Ex. at 60-61. No party raised an objection to the CAD adjustments.

The Commission adopts the CAD adjustments as a reasonable treatment to recognize the availability of customer deposits while compensating Hope for the cost of the capital it holds as customer deposits.

#### 9. Rent Expenses

The parties initially disagreed over an adjustment Hope made regarding expenses for facilities Hope uses in Weston and Clarksburg. Staff initially recommended an adjustment of \$123,896 that included a new lease for the Clarksburg facility but excluded any costs for a Weston facility. Staff Ex. 6A at 22. CAD also recommended removing any cost allowance for the Weston facility and

to justify. While CAD recommended against including 100% of the local dues, it recommended retaining 60% of AGA dues. CAD justified the split on AGA dues with an audit from the National Association of Regulatory Utility Commissioners ("NARUC") showing that approximately 40% of AGA expenses are applied to uses such as lobbying, advocacy or promotional activities. Based on the NARUC audit, CAD recommended removing \$10,831 in AGA dues. Together with the reduction CAD recommended for local dues, it recommended a total reduction of \$24,214 in dues costs from the Commission cost of service calculation. CAD Ex. 9 at 70-74.

Hope objected to the CAD recommendation in rebuttal testimony, arguing that these local organizations provide contacts that assist in attracting and maintaining customers. It also argued that the AGA provides useful operational assistance, helps Hope by monitoring legislative development and promotes the natural gas industry. Hope Ex. 10 at 16-17.

The Commission adopts the CAD position regarding AGA dues. Splitting the cost between ratepayers and shareholders on the basis of the amount of AGA dues applied to functions related to delivery of natural gas is a reasonable allocation method. The Commission also agrees with CAD that Hope has not provided specific information to justify finding that dues in local chambers of commerce are a cost of providing natural gas service. The Commission reduces the Hope expenses for these items by \$24,214, including disallowance of local dues and 40% of Hope AGA dues.

#### 14. DRS Charges

CAD and Staff challenged a number of expenses Hope included in its going level expenses that Dominion Resources Services, Inc. ("DRS"), the Dominion service company, billed to Hope. CAD recommended disallowing eight separate categories of DRS charges totaling \$364,570 in costs including (i) 50% of incentive compensation to senior management provided through DRS, (ii) membership dues, (iii) lobbying expenses, (iv) public relations expenses, (v) charitable contributions, (vi) social club dues, (vii) corporate sponsored sporting events and (viii) \$134,979 in corporate aviation costs. CAD Ex. 9 at 77-78. CAD argued that the expenses, except for incentive compensation, are not required for providing gas service and do not benefit ratepayers. CAD Initial Brief at 100. CAD split the incentive compensation charge as a reflection of the shared benefit of incentive compensation to both shareholders and ratepayers. Staff also recommended that the Commission eliminate a similar list of expenses (except for aviation charges) for a total of \$378,831. Staff Ex. 13 at 16-17. Staff asserted that Dominion stockholders benefit from these expenses and therefore should bear them. Id.

Hope objected to the CAD and Staff recommendations regarding the protested DRS charges. Hope argued that the incentive compensation charges from DRS are a necessary part of the package Dominion uses to attract and retain talented executives. It defended the aviation charges as legitimate expenses that are individually charged on the basis of each flight. Hope justified the media expenses DRS charged, asserting that those expenses support the office within Dominion that maintains copies of current tariffs and prepares bill inserts, including any required by Commission rules. Hope Ex. 13 at 16-17. Hope did not specifically address the recommendations regarding expenses including social club dues and sports tickets. See, Case file generally.

The Commission believes that these costs from DRS are not directly related to Hope providing reliable natural gas service to its customers. The Commission fails to see how membership dues, social club dues and sports tickets substantially enhance service to customers. Evidence in the record regarding corporate aviation charges is also insufficient to justify including those expenses in the revenue requirement calculations. The Commission is also not convinced that Dominion lobbying efforts benefit Hope ratepayers and agrees with the recommendation to disallow those costs.

The Commission has no desire to dissuade Hope or any utility from making reasonable charitable contributions to the communities they serve, but believes that charitable donations are a cost that should be borne by shareholders who can influence decisions regarding support to charitable organizations, and not by ratepayers that have no say in those decisions. The Commission will not accept the DRS charges for charitable contributions to Hope. The Commission notes that it distinguishes the Targeted Gas Energy Efficiency Program ("T/GEEP") from other charitable contributions and discusses that program separately below.

Hope did make a brief reference in testimony regarding the use of media expenses, noting that the recipient of those costs maintain current tariffs and prepare bill inserts. The record does not indicate, however, any specific benefits of those fees, and the Commission views any DRS costs associated with maintaining current tariffs skeptically. The Commission cannot accept DRS charges for media affairs based on the record.

The Commission accepts the Staff recommendation regarding incentive compensation expenses for senior management charged by DRS to Hope. As noted by Mr. McKeown, Hope has no senior management of its own and relies on DRS to provide those functions. While the Commission is sympathetic to the desires of Hope to attract and retain talented employees, Hope executives should consider the current economic climate in their bonus requests. As discussed above regarding merit increases for other salary employees, the Commission cannot justify bonus costs for Hope executives in the midst of protracted economic turmoil. The Commission disallows the DRS charges listed above removing \$378,831 Staff recommended plus \$134,979 in aviation costs for a total of \$513,810 from the cost of service calculations.

#### 15. Adjustments for Hope Addendum

CAD recommended a net adjustment reducing expenses by \$2,096 to account for the tax implications of removing the post test year additions to rate base in the addendum to Statement B discussed above in the rate base section. CAD Ex. 9 at 80 and CAD Initial Brief at 102. Similarly, Hope requested adjustments to reflect the addendum additions it proposed including \$867,123 for depreciation, depletion and amortization expenses related to including the addendum plant in rate base and \$145,274 adjustment to tax expenses. Hope Initial Brief at 41. The Commission adopts the CAD adjustment to synchronize the cost of service as consistent with its decision to exclude the post test year addendum items from rate base consideration and denies the Hope adjustments on similar grounds.

**COMPANY:** ARIZONA AMERICAN WATER COMPANY  
**DOCKET NO:** W-01303A-09-0343; SW-01303A-09-0343

**Response provided by:** Tom Broderick

**Title:** Director, Rates & Regulation

**Address:** 2355 W. Pinnacle Peak Road, Suite 300  
Phoenix, AZ 85027

**Company Response Number:** RUCO 7-1

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- Q. Pension expense from affiliates. Refer to AAWC's response to RUCO 2-61. (a) Please explain the unusually large charge in December 2006 of \$1,304,179 for Account 506100, Pension, from the affiliated Service Company. (b) Please provide the journal entries, and journal entry support, for the affiliated Service Company charges to Account 506100, Pensions for December 2006. (c) Was the unusually large charge in December 2006 of \$1,304,179 for Account 506100, Pension, from the affiliated Service Company addressed in any prior AAWC rate case? If not, explain fully why not. If so, please identify the specific rate cases in which this was addressed, and explain how it was addressed.
- A: a) This is when the Service Company began to bill pension cost based on FAS 87 instead of ERISA. For an ERISA state such as AZ, there was an offsetting debit to expense and credit to a regulatory asset for the difference between accruals (FAS 87) and contributions (ERISA).
- b) Please see Attachment RUCO 7-1 Pension Expense from Affiliates.xls. The \$1,304,179 balance in account 506100 for December 2006 as shown on AAWC's response to RUCO 2-61 includes the standard monthly Pension entry as well as the \$1,274,913 transition entry. The journal entry is displayed on the Pension JE tab of the attachment.
- c) AAWC has remained an ERISA state for ratemaking purposes. For AAWC, the issue has not been revisited since the ACC's 1993 Decision No. 58419. AAWC continues to debit a regulatory asset for the on-going difference between pension accruals and contributions.